



Office of the Washington State Auditor
Pat McCarthy

Financial Statements Audit Report

City of Mercer Island

For the period January 1, 2023 through December 31, 2023

Published December 12, 2024

Report No. 1036042



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**Office of the Washington State Auditor
Pat McCarthy**

December 12, 2024

Council
City of Mercer Island
Mercer Island, Washington

Report on Financial Statements

Please find attached our report on the City of Mercer Island's financial statements.

We are issuing this report in order to provide information on the City's financial activities and condition.

Sincerely,

Pat McCarthy, State Auditor
Olympia, WA

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TABLE OF CONTENTS

Summary Schedule of Prior Audit Findings	4
Independent Auditor's Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	6
Independent Auditor's Report on the Financial Statements.....	9
Financial Section.....	13
About the State Auditor's Office.....	40



SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

City of Mercer Island January 1, 2023 through December 31, 2023

This schedule presents the status of findings reported in prior audit periods.

Audit Period: January 1, 2022 through December 31, 2022	Report Ref. No.: 1034826	Finding Ref. No.: 2022-001
Finding Caption: The City's internal controls were inadequate for ensuring proper revenue recognition for funds received in advance.		
Background: During 2022, the City received \$3,617,659 in federal financial assistance from the Coronavirus State and Local Fiscal Recovery Funds, which is a program funded through the American Rescue Plan Act of 2021 (ARPA). During the audit period, the City incurred eligible program expenditures of \$1,070,885. In this instance the City received Coronavirus State and Local Fiscal Recovery funds before it incurred eligible expenditures. However, the City did not properly evaluate whether it met revenue recognition criteria for grants it received in advance. Specifically, the City misinterpreted the revenue recognition criteria for the unspent funds, which should be reported as unearned revenue, a liability, until it meets the applicable eligibility requirements.		
Status of Corrective Action: (check one) <input checked="" type="checkbox"/> Fully Corrected <input type="checkbox"/> Partially Corrected <input type="checkbox"/> Not Corrected <input type="checkbox"/> Finding is considered no longer valid		
Corrective Action Taken: <i>The 2022 Financial statements were corrected prior to the final audit report being issued per the instructions of the State Audit Office. The statement below was published with the final audit report.</i> <i>For the benefit of Mercer Island residents, this matter does not represent any misuse of public funds. Rather, it represents a reporting error involving how the federal funds received were classified for audit reports. The City utilized the guidance from the State Auditor's Office</i>		

(SAO) along with resources from the US Treasury for State and Local Fiscal Recovery Funds, the Government Finance Officers Association (GFOA), and Governmental Accounting Standards Board (GASB) in determining ARPA reporting requirements. The US Treasury's guidance for distributions to non-entitlement units (NEU) of local government prohibited States from disbursing funds to NEUs on a reimbursement basis. The State Auditors BARS manual and the remittance advice from the Washington State Treasurer's Office both indicated ARPA revenues be coded as "federal revenues, other than grants." On this basis, the City did not consider ARPA funds an expenditure based reimbursable grant throughout the financial statement evaluation and review process. Absent specific direction from the SAO, Management elected to recognize earned revenue as ARPA funds were committed for eligible uses by the City Council. The decision to recognize earned revenue as ARPA funds were committed was discussed in length with the SAO audit team during the 2021 annual financial audit. The audit team gave no indication the City's revenue recognition determination was non-compliant with Generally Accepted Accounting Principles (GAAP). Given fiscal year 2021 audit results, the City used the same revenue recognition criteria in the 2022 annual financial statements. Staff acknowledges that the City's interpretation of the revenue recognition criteria for ARPA funds was inconsistent with that of the SAO. However, the City believes adequate controls and procedures are in place and disagrees with the assessment of a material weakness in internal controls. Once advised of the appropriate revenue recognition criteria for ARPA funds, the City corrected amounts reported in earned and unearned revenue classifications in the 2022 financial statements. Had this explanation been provided in the first year of ARPA reporting (2021), this finding would have been avoided.

INDEPENDENT AUDITOR'S REPORT

Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

City of Mercer Island January 1, 2023 through December 31, 2023

Council
City of Mercer Island
Mercer Island, Washington

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the City of Mercer Island, as of and for the year ended December 31, 2023, and the related notes to the financial statements, which collectively comprise the City's financial statements, and have issued our report thereon dated December 3, 2024.

We issued an unmodified opinion on the fair presentation of the City's financial statements in accordance with its regulatory basis of accounting. We issued an adverse opinion on the fair presentation with regard to accounting principles generally accepted in the United States of America (GAAP) because the financial statements are prepared by the City using accounting practices prescribed by state law and the State Auditor's *Budgeting, Accounting and Reporting System* (BARS) manual described in Note 1, which is a basis of accounting other than GAAP. The effects on the financial statements of the variances between the basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) as a basis for designing audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the City's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described above and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified.

Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses.

REPORT ON COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the financial statements. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

PURPOSE OF THIS REPORT

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this

report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink that reads "Pat McCarthy". The signature is written in a cursive style with a large, sweeping initial "P".

Pat McCarthy, State Auditor

Olympia, WA

December 3, 2024

INDEPENDENT AUDITOR'S REPORT

Report on the Audit of the Financial Statements

City of Mercer Island January 1, 2023 through December 31, 2023

Council
City of Mercer Island
Mercer Island, Washington

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

Unmodified and Adverse Opinions

We have audited the financial statements of the City of Mercer Island, as of and for the year ended December 31, 2023, and the related notes to the financial statements, as listed in the financial section of our report.

Unmodified Opinion on the Regulatory Basis of Accounting (BARS Manual)

As described in Note 1, the City has prepared these financial statements to meet the financial reporting requirements of state law and accounting practices prescribed by the State Auditor's *Budgeting, Accounting and Reporting System* (BARS) Manual. Those accounting practices differ from accounting principles generally accepted in the United States of America (GAAP). The differences in these accounting practices are also described in Note 1.

In our opinion, the accompanying financial statements referred to above present fairly, in all material respects, the cash and investments of the City of Mercer Island, and its changes in cash and investments, for the year ended December 31, 2023, on the basis of accounting described in Note 1.

Adverse Opinion on U.S. GAAP

The financial statements referred to above were not intended to, and in our opinion, they do not, present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the City of Mercer Island, as of December 31, 2023, or the changes in financial position or cash flows thereof for the year then ended, because of the significance of the matter discussed below.

Basis for Unmodified and Adverse Opinions

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS) and *Government Auditing Standards*. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the City, and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit unmodified and adverse opinions.

Matter Giving Rise to Adverse Opinion on U.S. GAAP

Auditing standards issued by the American Institute of Certified Public Accountants (AICPA) require auditors to formally acknowledge when governments do not prepare their financial statements, intended for general use, in accordance with GAAP. As described in Note 1 of the financial statements, the financial statements are prepared by the City in accordance with state law using accounting practices prescribed by the BARS Manual, which is a basis of accounting other than accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between the regulatory basis of accounting and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material and pervasive.

Matters of Emphasis

As discussed in Note 7 to the financial statements, the City elected to change its method of accounting from generally accepted accounting principles to a special purpose framework during the year ended December 31, 2023.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the financial reporting provisions of state law and the BARS Manual described in Note 1. This includes determining that the basis of accounting is acceptable for the presentation of the financial statements in the circumstances. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the City's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

Performing an audit in accordance with GAAS and *Government Auditing Standards* includes the following responsibilities:

- Exercise professional judgment and maintain professional skepticism throughout the audit;
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements;
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, no such opinion is expressed;
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements;
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the City's ability to continue as a going concern for a reasonable period of time; and
- We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the City's financial statements. The Schedule of Liabilities is presented for purposes of additional analysis, as required by the prescribed BARS manual. This schedule is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to

prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the financial statements as a whole.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated December 3, 2024 on our consideration of the City's internal control over financial reporting and on the tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.



Pat McCarthy, State Auditor

Olympia, WA

December 3, 2024

**City of Mercer Island
January 1, 2023 through December 31, 2023**

FINANCIAL STATEMENTS

Fund Resources and Uses Arising from Cash Transactions – 2023
Fiduciary Fund Resources and Uses Arising from Cash Transactions – 2023
Notes to Financial Statements – 2023

SUPPLEMENTARY AND OTHER INFORMATION

Schedule of Liabilities – 2023

City of Mercer Island
Fund Resources and Uses Arising from Cash Transactions
For the Year Ended December 31, 2023

		Total for All Funds (Memo Only)	001 General Fund	104 Street Fund	160 Youth & Family Services Fund
Beginning Cash and Investments					
308	Beginning Cash and Investments	79,827,769	17,524,763	5,828,791	476,613
388 / 588	Net Adjustments	-	-	-	-
Revenues					
310	Taxes	31,636,907	26,491,673	1,909,517	40,008
320	Licenses and Permits	3,384,466	3,384,466	-	-
330	Intergovernmental Revenues	4,376,760	982,911	2,664,787	266,125
340	Charges for Goods and Services	35,020,843	3,992,767	148,397	1,720,958
350	Fines and Penalties	221,719	221,719	-	-
360	Miscellaneous Revenues	5,801,156	3,658,963	-	393,441
Total Revenues:		<u>80,441,851</u>	<u>38,732,499</u>	<u>4,722,701</u>	<u>2,420,532</u>
Expenditures					
510	General Government	9,500,187	7,734,721	-	-
520	Public Safety	17,043,891	17,011,438	-	-
530	Utilities	18,846,066	-	-	-
540	Transportation	3,082,966	1,172,214	1,333,590	-
550	Natural/Economic Environment	3,844,269	3,376,065	-	-
560	Social Services	3,249,460	64,623	-	3,184,837
570	Culture and Recreation	4,714,343	4,714,343	-	-
Total Expenditures:		<u>60,281,182</u>	<u>34,073,404</u>	<u>1,333,590</u>	<u>3,184,837</u>
Excess (Deficiency) Revenues over Expenditures:		20,160,669	4,659,095	3,389,111	(764,305)
Other Increases in Fund Resources					
391-393, 596	Debt Proceeds	-	-	-	-
397	Transfers-In	2,164,638	-	139,574	864,790
385	Special or Extraordinary Items	-	-	-	-
381, 382, 389, 395, 398	Other Resources	255,113	-	-	-
Total Other Increases in Fund Resources:		<u>2,419,751</u>	<u>-</u>	<u>139,574</u>	<u>864,790</u>
Other Decreases in Fund Resources					
594-595	Capital Expenditures	19,480,790	39,940	3,116,583	37,506
591-593, 599	Debt Service	1,518,499	142,498	-	-
597	Transfers-Out	2,152,638	1,257,433	-	-
585	Special or Extraordinary Items	-	-	-	-
581, 582, 589	Other Uses	213,023	195,507	-	-
Total Other Decreases in Fund Resources:		<u>23,364,950</u>	<u>1,635,378</u>	<u>3,116,583</u>	<u>37,506</u>
Increase (Decrease) in Cash and Investments:		<u>(784,530)</u>	<u>3,023,717</u>	<u>412,102</u>	<u>62,979</u>
Ending Cash and Investments					
50821	Nonspendable	-	-	-	-
50831	Restricted	18,730,443	727,890	5,908,607	42,447
50841	Committed	3,052,824	1,047,826	232,607	497,145
50851	Assigned	40,875,768	2,388,558	99,684	-
50891	Unassigned	16,384,202	16,384,202	-	-
Total Ending Cash and Investments		<u>79,043,237</u>	<u>20,548,476</u>	<u>6,240,898</u>	<u>539,592</u>

The accompanying notes are an integral part of this statement.

City of Mercer Island
Fund Resources and Uses Arising from Cash Transactions
For the Year Ended December 31, 2023

		170 ARPA Fund	208 Bond Redemption Voted Fund	239 Bond Redemption Non-Voted Fund	342 Town Center Parking Facilities Fund
Beginning Cash and Investments					
308	Beginning Cash and Investments	6,052,052	18,943	5,038	708,593
388 / 588	Net Adjustments	-	-	-	-
Revenues					
310	Taxes	-	-	-	-
320	Licenses and Permits	-	-	-	-
330	Intergovernmental Revenues	-	-	-	-
340	Charges for Goods and Services	-	-	-	-
350	Fines and Penalties	-	-	-	-
360	Miscellaneous Revenues	-	-	42	-
Total Revenues:		-	-	42	-
Expenditures					
510	General Government	449,796	-	-	-
520	Public Safety	-	-	-	-
530	Utilities	198,123	-	-	-
540	Transportation	-	-	-	-
550	Natural/Economic Environment	9,102	-	-	-
560	Social Services	-	-	-	-
570	Culture and Recreation	-	-	-	-
Total Expenditures:		657,021	-	-	-
Excess (Deficiency) Revenues over Expenditures:		(657,021)	-	42	-
Other Increases in Fund Resources					
391-393, 596	Debt Proceeds	-	-	-	-
397	Transfers-In	-	-	142,800	-
385	Special or Extraordinary Items	-	-	-	-
381, 382, 389, 395, 398	Other Resources	-	-	-	-
Total Other Increases in Fund Resources:		-	-	142,800	-
Other Decreases in Fund Resources					
594-595	Capital Expenditures	-	-	-	-
591-593, 599	Debt Service	27,015	-	142,800	-
597	Transfers-Out	522,343	-	-	-
585	Special or Extraordinary Items	-	-	-	-
581, 582, 589	Other Uses	-	-	-	-
Total Other Decreases in Fund Resources:		549,358	-	142,800	-
Increase (Decrease) in Cash and Investments:		(1,206,379)	-	42	-
Ending Cash and Investments					
50821	Nonspendable	-	-	-	-
50831	Restricted	4,845,674	-	-	202,196
50841	Committed	-	-	-	-
50851	Assigned	-	18,943	5,080	506,397
50891	Unassigned	-	-	-	-
Total Ending Cash and Investments		4,845,674	18,943	5,080	708,593

The accompanying notes are an integral part of this statement.

City of Mercer Island
Fund Resources and Uses Arising from Cash Transactions
For the Year Ended December 31, 2023

		343 Capital Improvement Fund	345 Technology & Equipment Fund	350 Facility Reserve Fund	402 Water Fund
Beginning Cash and Investments					
308	Beginning Cash and Investments	8,207,738	1,588,924	-	19,747,543
388 / 588	Net Adjustments	-	-	-	-
Revenues					
310	Taxes	3,029,100	-	-	-
320	Licenses and Permits	-	-	-	-
330	Intergovernmental Revenues	387,937	-	-	-
340	Charges for Goods and Services	260,730	-	-	11,877,832
350	Fines and Penalties	-	-	-	-
360	Miscellaneous Revenues	-	-	-	968,775
Total Revenues:		3,677,767	-	-	12,846,607
Expenditures					
510	General Government	299,194	-	-	-
520	Public Safety	-	32,453	-	-
530	Utilities	-	-	-	7,252,945
540	Transportation	-	-	-	-
550	Natural/Economic Environment	-	-	-	-
560	Social Services	-	-	-	-
570	Culture and Recreation	-	-	-	-
Total Expenditures:		299,194	32,453	-	7,252,945
Excess (Deficiency) Revenues over Expenditures:		3,378,573	(32,453)	-	5,593,662
Other Increases in Fund Resources					
391-393, 596	Debt Proceeds	-	-	-	-
397	Transfers-In	53,916	280,000	579,808	-
385	Special or Extraordinary Items	-	-	-	-
381, 382, 389, 395, 398	Other Resources	-	-	-	133,251
Total Other Increases in Fund Resources:		53,916	280,000	579,808	133,251
Other Decreases in Fund Resources					
594-595	Capital Expenditures	3,743,190	563,772	-	8,075,414
591-593, 599	Debt Service	-	30,978	-	117,156
597	Transfers-Out	142,800	-	-	32,976
585	Special or Extraordinary Items	-	-	-	-
581, 582, 589	Other Uses	-	-	-	17,516
Total Other Decreases in Fund Resources:		3,885,990	594,750	-	8,243,062
Increase (Decrease) in Cash and Investments:		(453,501)	(347,203)	579,808	(2,516,149)
Ending Cash and Investments					
50821	Nonspendable	-	-	-	-
50831	Restricted	6,962,284	41,345	-	-
50841	Committed	36,793	-	579,808	-
50851	Assigned	755,162	1,200,377	-	17,231,392
50891	Unassigned	-	-	-	-
Total Ending Cash and Investments		7,754,239	1,241,722	579,808	17,231,392

The accompanying notes are an integral part of this statement.

City of Mercer Island
Fund Resources and Uses Arising from Cash Transactions
For the Year Ended December 31, 2023

		426 Sewer Fund	432 Stormwater Fund	503 Equipment Rental Fund	520 Computer Equipment Fund
Beginning Cash and Investments					
308	Beginning Cash and Investments	9,675,256	4,585,398	4,573,908	834,209
388 / 588	Net Adjustments	-	-	-	-
Revenues					
310	Taxes	-	-	166,609	-
320	Licenses and Permits	-	-	-	-
330	Intergovernmental Revenues	-	75,000	-	-
340	Charges for Goods and Services	12,038,797	2,629,971	1,080,747	1,270,644
350	Fines and Penalties	-	-	-	-
360	Miscellaneous Revenues	509,622	237,976	32,337	-
Total Revenues:		12,548,419	2,942,947	1,279,693	1,270,644
Expenditures					
510	General Government	-	-	-	1,016,476
520	Public Safety	-	-	-	-
530	Utilities	9,067,914	2,327,084	-	-
540	Transportation	-	-	577,162	-
550	Natural/Economic Environment	-	-	459,102	-
560	Social Services	-	-	-	-
570	Culture and Recreation	-	-	-	-
Total Expenditures:		9,067,914	2,327,084	1,036,264	1,016,476
Excess (Deficiency) Revenues over Expenditures:		3,480,505	615,863	243,429	254,168
Other Increases in Fund Resources					
391-393, 596	Debt Proceeds	-	-	-	-
397	Transfers-In	-	-	103,750	-
385	Special or Extraordinary Items	-	-	-	-
381, 382, 389, 395, 398	Other Resources	97,607	-	24,255	-
Total Other Increases in Fund Resources:		97,607	-	128,005	-
Other Decreases in Fund Resources					
594-595	Capital Expenditures	2,821,845	306,265	661,731	114,544
591-593, 599	Debt Service	1,041,867	7,625	-	8,560
597	Transfers-Out	52,440	144,646	-	-
585	Special or Extraordinary Items	-	-	-	-
581, 582, 589	Other Uses	-	-	-	-
Total Other Decreases in Fund Resources:		3,916,152	458,536	661,731	123,104
Increase (Decrease) in Cash and Investments:		(338,040)	157,327	(290,297)	131,064
Ending Cash and Investments					
50821	Nonspendable	-	-	-	-
50831	Restricted	-	-	-	-
50841	Committed	-	-	658,645	-
50851	Assigned	9,337,214	4,742,725	3,624,965	965,271
50891	Unassigned	-	-	-	-
Total Ending Cash and Investments		9,337,214	4,742,725	4,283,610	965,271

The accompanying notes are an integral part of this statement.

City of Mercer Island
Fiduciary Fund Resources and Uses Arising from Cash Transactions
For the Year Ended December 31, 2023

		Total for All Funds (Memo Only)	Pension/OPEB Trust Fund	Custodial
308	Beginning Cash and Investments	1,064,448	1,032,149	32,299
388 & 588	Net Adjustments	-	-	-
310-390	Additions	778,325	118,630	659,695
510-590	Deductions	766,036	111,833	654,203
	Net Increase (Decrease) in Cash and Investments:	12,289	6,797	5,492
508	Ending Cash and Investments	1,076,738	1,038,947	37,791

The accompanying notes are an integral part of this statement.

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The City of Mercer Island was incorporated on July 18, 1960. It remained separate from the Town of Mercer Island (which occupied the area now in the central business district) until July of 1970. The City has a council-manager form of government and operates under Title 35A of the Revised Code of Washington (RCW). The City Council is composed of seven non-partisan members elected at large for 4-year terms. From among the council members a mayor is elected for a term of two years. Day-to-day City operations are under the direction of a city manager, who is appointed by the council. The City provides general government services including police, streets and trails, parks and recreation, planning and zoning, permits and inspection, general administrative and water, sewer, and storm water services.

The city reports financial activity in accordance with the Cash Basis Budgeting, Accounting and Reporting System (BARS) Manual prescribed by the State Auditor's Office under the authority of Washington State law, Chapter 43.09 RCW. This manual prescribes a financial reporting framework that differs from Generally Accepted Accounting Principles (GAAP) in the following manner:

- Financial transactions are recognized on a cash basis of accounting as described below.
- Component units are required to be disclosed, but are not included in the financial statements (see Note 8 – Joint Ventures, and Related Parties).
- Government-wide statements, as defined in GAAP, are not presented.
- All funds are presented, rather than a focus on major funds.
- The Schedule of Liabilities is required to be presented with the financial statements as supplementary information.
- Supplementary information required by GAAP is not presented.
- Ending balances for proprietary and fiduciary funds are presented using classifications that are different from the ending net position classifications in GAAP.

A. Fund Accounting

Financial transactions of the government are reported in individual funds. Each fund uses a separate set of self-balancing accounts that comprises its cash and investments, revenues and expenditures. The government's resources are allocated to and accounted for in individual funds depending on their intended purpose. Each fund is reported as a separate column in the financial statements, except for fiduciary funds, which are presented by fund types. The total column is presented as "memo only" because any interfund activities are not eliminated. The following fund types are used:

GOVERNMENTAL FUND TYPES

The **General Fund** is the primary operating fund of the government. It accounts for all financial resources except those required or elected to be accounted for in another fund.

Special Revenue Funds account for specific revenue sources that are restricted or committed to expenditures for specified purposes of the government.

Debt Service Funds account for the financial resources that are restricted, committed, or assigned to expenditures for principal, interest and related costs on general long-term debt.

Capital Project Funds account for financial resources which are restricted, committed, or assigned for the acquisition or construction of capital facilities or other capital assets.

PROPRIETARY FUND TYPES

Enterprise Funds account for operations that provide goods or services to the general public and are supported primarily through user charges.

Internal Service Funds account for operations that provide goods or services to other departments or funds of the government on a cost reimbursement basis.

FIDUCIARY FUND TYPES

Fiduciary funds account for assets held by the government in a trustee capacity or as a custodian on behalf of others.

Pension Trust Funds are used to report fiduciary activities for pension plans administered through trust.

Custodial Funds are used to account for assets that the government holds on behalf of others in a custodial capacity.

B. Basis of Accounting and Measurement Focus

Financial statements are prepared using the cash basis of accounting and measurement focus. Revenues are recognized when cash is received, and expenditures are recognized when paid. In accordance with state law the City also recognizes expenditures paid during twenty days after the close of the fiscal year for claims incurred during the previous period.

C. Cash and Investments

See Note 3 – Deposits and Investments.

D. Capital Assets

Capital assets are assets with an initial individual cost of more than \$10,000 and an estimated useful life in excess of two years. Capital assets and inventory are recorded as capital expenditures or supplies as appropriate when purchased.

E. Compensated Absences

Vacation leave for permanent full-time employees accumulates monthly at annual rates ranging from 12 to 21 days unless otherwise provided for in a collective bargaining agreement. Permanent part-time employees who work at least 8 hours per week earn vacation leave on a pro-rata basis. Employees with at least 5 years and 10 years of service may convert respectively 3 and 5 days of accrued vacation leave to cash, paid through the regular payroll. At termination of employment, employees with the required length of service may receive cash payment for accumulated vacation leave up to a maximum of 30 days. The payment is based on current wages at termination. Payments are recognized as expenditures when paid.

Sick leave for permanent full-time employees accumulates monthly at the rate of one day for each full month of service unless otherwise provided in a collective bargaining agreement. Permanent part-time employees who work at least 8 hours per week earn sick leave on a pro-rata basis. Sick leave can be

accrued to a maximum of 90 days; however, no compensation for accrued sick leave is paid on termination.

F. Long-Term Debt

See Note 10 – Long-term Debt.

G. Restricted and Committed Portion of Ending Cash and Investments

Beginning and Ending Cash and Investments are reported as restricted or committed when it is subject to restrictions on use imposed by external parties or due to internal commitments established by the City Council. When expenditures that meet restrictions are incurred, the City intends to use the most restricted resources first.

	General	Special Revenue	Debt Service	Capital Projects	Enterprise	Fuduciary	Total
Restricted							
Capital investment in parks, buildings and open space				358,291			358,291
American Rescue Plan Act		4,845,674					4,845,674
ENTF Drug enforcement & education				41,345			41,345
National Opiate Settlement		42,447					42,447
Law enforcement training	81,793						81,793
KC parks expansion levy funds				569,790			569,790
REET 1 and REET 2		5,908,607		6,236,399			12,145,006
Sound Transit Airspace Agreement	646,097						646,097
Pension Trust						1,038,947	1,038,947
Custodial Deposits						37,791	37,791
Total Restricted	\$ 727,890	\$ 10,796,728	\$ -	\$ 7,205,825	\$ -	\$ 1,076,738	\$ 19,807,181
Committed							
Art in public places	155,186						155,186
GMA Impact Parks, streets, paths and trails		232,607		36,793			269,400
Human services		497,145					497,145
LEOFF 1 long term care	852,640						852,640
Self insurance	40,000						40,000
Fire Apparatus					658,645		658,645
Facility Replacement				579,808			579,808
Total Committed	\$ 1,047,826	\$ 729,752	\$ -	\$ 616,601	\$ 658,645	\$ -	\$ 3,052,824

NOTE 2 – BUDGET COMPLIANCE

The City adopts biennial appropriated budgets for general, special revenue, debt service, enterprise, internal service and pension trust funds. These budgets are appropriated at the fund level. The budget constitutes the legal authority for expenditures at the fund level. Biennial appropriations for these funds lapse at the end of the biennium.

Biennial appropriated budgets are adopted on the same basis of accounting as used for financial reporting.

The appropriated and actual expenditures for the legally adopted budgets were as follows:

Fund Type / Fund Name (\$ in Million)	Original Adopted Budget	Budget Adjustments	Final Budget	Actual Expenditures	Variance
General Purpose Funds:					
General	\$ 71.02	\$ 7.92	\$ 78.93	\$ 35.44	\$ 43.49
Self-Insurance	0.02	-	0.02	-	0.02
Contingency	-	0.22	0.22	0.22	-
1% for the Arts	0.03	0.07	0.10	0.05	0.05
Special Revenue Funds:					
Street	14.80	2.41	17.21	4.45	12.76
Youth & Family Services	6.69	0.21	6.90	3.22	3.68
ARPA Funds	3.24	2.23	5.47	1.21	4.27
Debt Service Funds:					
Bond Redemption (Voted)	-	-	-	-	-
Bond Redemption (Non-Voted)	0.14	-	0.14	0.14	-
Capital Projects Funds:					
Town Center Parking Facilities	-	-	-	-	-
Capital Improvement	21.79	0.60	22.38	4.19	18.20
Technology & Equipment	0.64	0.71	1.35	0.63	0.72
Facility Reserve	-	-	-	-	-
Enterprise Funds:					
Water	42.79	11.51	54.30	15.50	38.80
Sewer	27.80	2.36	30.16	12.98	17.18
Stormwater	6.87	0.17	7.04	2.79	4.26
Internal Service Funds:					
Equipment Rental	2.99	0.74	3.73	1.70	2.03
Computer Equipment	2.47	-	2.47	1.14	1.33
Pension Trust Funds:					
Firefighter's Pension	0.20	0.04	0.24	0.11	0.13
Total (\$ in Millions)	\$ 201.49	\$ 29.18	\$ 230.67	\$ 83.76	\$ 146.91

Budget adjustments are made periodically throughout the year when changes in fund appropriations are necessary. Transfers between departments within any one fund may be made by order of the City Manager. Any revisions that alter the total expenditure of a fund must be approved by the City Council.

Intrafund transfers, or transfers within the same fund, are also included in the total adopted budgets for managerial control but have been excluded from actual expenditures.

NOTE 3 – DEPOSITS AND INVESTMENTS

Investments are reported at original cost. Deposits and Investments at December 31, 2023 are as follows:

Type of deposit or investment	City's own deposits and investments	Deposits and investments held by the City as custodian for other local government, individuals, or private organizations.	Total
Bank Deposits and LGIP	\$ 79,043,235	\$ 1,076,738	\$ 80,119,974
	\$ 79,043,235	\$ 1,076,738	\$ 80,119,974

It is the City’s policy to invest all temporary cash surpluses. The interest on these investments is allocated to the various funds per Council policy.

Investments in the State Local Government Investment Pool (LGIP)

The City is a voluntary participant in the Local Government Investment Pool, an external investment pool operated by the Washington State Treasurer. The pool is not rated and not registered with the SEC. Rather; oversight is provided by the State Finance Committee in accordance with Chapter 43.250 RCW. Investments in the LGIP are reported at amortized cost, which is the same as the value of the pool per share. The LGIP does not impose any restrictions on participant withdrawals.

The Office of the State Treasurer prepares a stand-alone financial report for the pool. A copy of the report is available from the Office of the State Treasurer, PO Box 40200, Olympia, Washington 98504-0200, or online at www.tre.wa.gov.

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in event of a failure of a depository financial institution, the City would not be able to recover deposits or would not be able to recover collateral securities that are in possession of an outside party. The City’s deposits and certificates of deposit are mostly covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

NOTE 4 – POLLUTION REMEDIATION OBLIGATIONS

In 1991 the City’s Maintenance Shop found a problem when it tested the “tightness” of its three underground storage tanks for unleaded gasoline and diesel fuel. A subsequent site investigation found minor problems but no failure of the three tanks or connecting piping. Soil samples, test pits and monitoring wells indicated that contamination was not widespread. A consultant’s report concluded that “the quantity of the petroleum released was probably quite small and poses little impact to the surrounding environment.”

The state Department of Ecology (DOE) recommended quarterly monitoring of three on-site monitoring wells. It is unclear from DOE and City records whether the City followed this recommendation. In June of 1993, the three tanks were removed along with an estimated 100 cubic yards of contaminated soils. Sampling of the excavation site found the soils removal was successful, but groundwater contamination was still present. The City installed an “air sparing/vapor extraction system” to remove groundwater contamination. Use of the system required a permit from the Puget Sound Air Pollution Control Agency. For reasons that are not known, the permit was never granted and the system was not activated.

In early July of 2004, the soils and groundwater of the site occupied by Honeywell International to the west and north of Maintenance Shop were tested as part of due diligence for a prospective sale of the property. The property is jointly owned by the Archdiocese of Seattle and two other out-of-state religious organizations. The consultants performing this testing found evidence of petroleum hydrocarbons and associated contaminants in soil and groundwater samples that exceeded state cleanup standards as defined by the Model Toxics Control Act. When notified of these results, the City hired Golder Associates to investigate. Golder conducted the original site investigation in 1991.

In two phases of work, Golder installed new monitoring wells, did soils borings, and tested the existing monitoring wells. Golder confirmed that the Maintenance Shop tanks were the only possible source of the petroleum contamination on the Honeywell site. Golder found that the contamination extended in groundwater beneath the Honeywell office building. Golder believes that petroleum contamination from the Maintenance Shop tanks may have migrated in groundwater to the Honeywell site along the original path of the stream that now flows generally east to west at the south end of the property. The course of the stream likely was altered to its present south to north flow prior to construction of the building occupied by Honeywell. The old stream channel is believed to be contained in a sandy layer between two impervious layers of clay and hard silt.

On Feb. 22, 2005, the City authorized Golder to begin a third phase of work that will define the precise extent of the petroleum contamination at the Honeywell site, test the indoor air in the Honeywell building to determine whether the contamination beneath the building is affecting air quality, begin removing petroleum contamination in groundwater, and recommend a plan for the final cleanup and monitoring of the Site.

The 2004-2005 remedial investigation found a gasoline groundwater plume extending north from the former underground tank site, under the former Honeywell building, and turning to the northeast toward City Hall.

Cleanup of the affected groundwater is required under the State Model Toxics Control Act (MTCA). Golder was asked to develop a conceptual remedial approach for cleanup of the groundwater plume. After the conceptual approach was presented to John Bails of the Washington State Department of Ecology (DOE)

and verbally approved, work began on a detailed plan for remediation. Following DOE acceptance, the remedial action plan as formalized and engineering design and compliance monitoring plans were completed in the summer of 2006.

The remedial action consisted of four components:

- Highly impacted groundwater was removed from the area north of the stream separating the Maintenance and Honeywell properties via excavation and the installation of an 80-foot-long by 10-foot-deep interceptor trench. The trench extracts impacted groundwater and pumps it to an activated carbon-based treatment system on the Maintenance property. After treatment, the water discharges to a King County/METRO sanitary sewer under discharge authorization number 4125-01.
- Approximately 260 cubic yards of highly contaminated soil were excavated from the south side of the Honeywell building.
- Biodegradation of the volatile organic compounds (VOCs) associated with the groundwater contamination plume has been enhanced by the introduction of ambient air via four buried airlines that intersect the gasoline plume and the application of oxidative chemicals.
- An existing network of monitoring wells to track the progress of the remediation was expanded. Short-term and long-term groundwater, surface water, and indoor air monitoring activities have been instituted.

In general, concentrations of gasoline and its VOC constituents remain above MTCA cleanup levels but appear to be decreasing with time. The property data for both sites showed progress in reducing the size of the plume, although test wells below the original fuel site still exceeded MTCA requirements. At the recommendation of Golder Associates, a pilot in-situ chemical oxidation test was implemented to accelerate the biodegradation of the contaminated groundwater.

In 2014, the City consulted with Farallon Consulting to complete a technical review of the remediation response, including the evaluation of the proposed pilot in-situ chemical oxidation test. Farallon recommended revamping the monitoring reports, including further descriptions of existing site conditions, cleanup activities, the evaluation of data, and moving from quarterly monitoring intervals to annual reports. Due to concerns over the effectiveness of the costly “in-situ” oxidation treatment, the City transitioned away from in-situ chemical applications in 2015 and 2016.

In compliance with the MTCA, the City continues to monitor and report on the remediation efforts annually. Remedial actions including the introduction of air into the subsurface to improve biological degradation continue. However, no chemical oxidation (Persulfate injections) are currently scoped. Golder also continues to maintain the remediation system and provide administrative support to complete the King County Metro discharge authorization permit and the DOE monitoring reports.

At significant points during this process, the City has consulted with the State Department of Ecology (DOE) and confirmed that the work being undertaken is appropriate and meets regulatory requirements. DOE has informed the City that the cleanup and monitoring process likely won't be completed for three to five years. DOE's Voluntary Compliance Program for underground storage tanks will allow the City to recover 50% of its costs, up to \$200,000, for the contamination investigation, clean-up and monitoring, following the issuance of a “No Further Action” letter at the completion of monitoring of the site.

NOTE 5 – ASSET RETIREMENT OBLIGATIONS

For the year ending December 31, 2020, the City implemented GASB Statement No. 83 Certain Retirement Obligations, which provides accounting and reporting guidance on asset retirement obligations. The City has the following known asset retirement obligations.

Emergency Water Well

The City is obligated by Washington Administrative Code (WAC) to take specific actions to decommission a water well in accordance with section WAC 173-160-381. The Code requires that the City take certain steps to permanently abandon a cased well including removal of liners, debris, sediments and obstruction; perforate and seal casings; and fill the casings. Engineering estimates set the cost of decommissioning the Water Utility emergency well at \$92,000 inclusive of sales tax and project management. This liability is reported on the schedule of liabilities.

Underground Fuel Tank

The City is obligated by Washington Administrative Code (WAC) to take specific actions when retiring underground storage tanks (UST's) in accordance with section WAC 173-360A-0810. The Code requires that the City take certain steps to permanently take USTs out of service including the removal, transportation and disposal of liquid, sludge, hazardous waste, as well as removal or capping of tanks and piping. Mercer Island currently has one underground fuel tank with a remaining useful life ranging from 0 to 5 years. The ARO for the underground tank is currently unknown. A site assessment is currently ongoing to determine if the underground tank is leaking fuel which would indicate the need for pollution remediation. If remediation steps are required, in addition to retirement costs, the estimated liability will be reported on the schedule of liabilities. During 2023 the City paid \$20,693 for related site assessment work.

Aquatic lease with Department of Natural Resources

The City is obligated by a lease agreement with the Department of Natural Resources (DNR) to remove all improvements to leased park land at the termination of the lease. Improvements include public buildings, public restrooms, waterfront plaza, fixed boat dock and pilings, fixed fishing pier, grated floating dock, grated steel gangway, bulkhead, treated pilings at swim beach, stormwater outfalls, recreation trails, and in-water buoys. The potential for termination of this lease is viewed as remote. The estimated cost of the asset retirement obligation liability for DNR aquatic lands is currently unknown, as such no liability is reported on the schedule of liabilities.

NOTE 6 – INTERFUND LOANS

At their regular meeting of September 15, 2020, the Mercer Island City Council authorized an interfund loan in the amount not to exceed \$750,000 from the Water Utility Fund to the General Fund, and an interfund loan in the amount not to exceed \$750,000 from the Sewer Utility Fund to the General Fund. The purpose of the interfund loans was to finance costs related to potential litigation to enforce the City’s terms of the 2017 Settlement Agreement with Sound Transit. The loans were initiated in November 2020 with a projected three-year repayment schedule with one-percent interest. The General Fund completed the repayment to both the Water Fund and the Sewer Fund in 2023.

Borrowing Fund	Lending Fund	Balance 01/01/2023	New Loans	Repayments	Balance 12/31/2023
General Fund	Water Fund	\$ 97,607	\$ -	\$ 97,607	\$ -
General Fund	Sewer Fund	97,607	-	97,607	-
Totals		\$ 195,214	\$ -	\$ 195,214	\$ -

NOTE 7 – CHANGE IN ACCOUNTING METHOD

In 2023, the City transitioned from Generally Accepted Accounting Principles (GAAP) to the cash basis of accounting for financial reporting as allowed by the Washington State Auditor’s Office (SAO) under the authority of RCW 43.09.200. The City employs the 20-day open period as prescribed by RCW 35.33.151. Beginning Cash balances for each fund were adjusted for transactions having cash impacts in 2023 but were originally reported in the prior year under GAAP to guarantee that the 2023 financial information includes a fair presentation of a full twelve months of regular operating revenues and expenses.

NOTE 8 – JOINT VENTURES

EPSCA

The Eastside Public Safety Communications Agency (EPSCA), an emergency regional radio access service provider operation, was established on May 26, 1992, by an interlocal agreement among the cities of Bellevue, Redmond, Kirkland and Mercer Island. The Agreement was amended in 1993, to include the City of Issaquah as an additional principal. EPSCA began principal operations in December 1995. In 2013 EPSCA was converted from an interlocal agency to a non-profit entity.

EPSCA is governed by an Executive Board, which is comprised of the Chief Executive officers of the Principals. The Executive Board is responsible for review and approval of all budgetary, financial, and contractual matters.

The current EPSCA emergency radio system is over 25 years old. In 2014, an Interlocal Cooperation Agreement was signed to provide for the implementation of a new regional emergency radio network system and will be paid for through a King County ballot measure approved by voters in 2015. The Puget Sound Emergency Radio Network (PSERN) is the intended successor and is expected to be complete in 2024. Budget monitoring and compiled financial statements for EPSCA can be obtained from EPSCA, c/o Kale Fong, MS PSEPS, PO Box 97010, Redmond WA 98073-9710.

E-Gov Alliance

In March 2002 the City of Mercer Island joined the Cities of Bellevue, Bothell, Burien, Issaquah, Kenmore, Kirkland, Sammamish and Woodinville in forming the E-Gov Alliance. The Alliance establishes on-line services through a jointly operated internet portal. Additionally, the Alliance has established a partnership with Microsoft to help define the E-Gov architecture, provide consulting services, offer training, and donated software.

The inter-local agreement may be terminated if Principals holding at least sixty percent (60%) of the weighted vote of all of the Principals are in concurrence. Upon termination, all property acquired shall be disposed of as follows: (1) property contributed without charge by any member shall revert to the contributor, (2) all property purchased after the effective date of the inter-local agreement shall be distributed to the Principals based upon each Principals proportional ownership interest at the time of the sale of the property. The City's share of the net position is deemed immaterial and thus is not reflected in the financial statements.

Budget monitoring information may be obtained from City of Bellevue, Information Technology Department, PO Box 90012, Bellevue, WA 98009.

NORCOM

In November of 2007, the City of Kirkland, with the cities of Bellevue, Bothell, Clyde Hill, Medina, Mercer Island, and Snoqualmie, along with Eastside Fire and Rescue, King County Fire Protection Districts 27 and 45, King and Kittitas County Fire Protection District 51, Northshore Fire Department, Shoreline Fire Department, and Woodinville Fire and Life Safety District entered into an interlocal agreement to establish and maintain a consolidated emergency service communications center. In 2008, the City of Redmond joined as a subscriber. Prior to the interlocal agreement, the formation efforts were carried out under a Joint Powers Agreement originally approved in 2005 and amended in 2006 and 2007. On July 1, 2009, the separate dispatch operations of the cities of Bellevue and Kirkland were combined and began operating as the Northeast King County Regional Public Safety Communications Agency (or NORCOM). NORCOM

includes 911 telephone answering, computer aided dispatch of fire, police and EMS resources, public safety field technology and a records management system.

Operating revenues are provided by user fees charged to each member based on average call volume. For 2023 the City of Mercer Island's share of these fees was \$748,048.

Additional financial information can be obtained from NORCOM, c/o Finance Manager, P.O. Box 50911, Bellevue, WA 98015.

ARCH – Housing Coalition

In November 1992, the cities of Bellevue, Kirkland, Redmond, and King County joined to establish A Regional Coalition for Housing (ARCH). The agreement was amended in January 1993 to add clarifying language regarding responsibility and disillusionment. Subsequently, the cities of Bothell, Issaquah, and Woodinville joined ARCH. Mercer Island joined ARCH in March 1994.

The purpose of ARCH is to cooperatively formulate affordable housing goals and policies and to foster efforts to provide affordable housing by combining public funding with private-sector resources. Operating funding is provided by the member cities. ARCH identifies and prioritizes projects which the member cities fund directly through their own grants, Community Development Block Grants, and HUD grants.

ARCH is governed by an Executive Board composed of the chief executive officer from each member agency. The Executive Board is responsible for review and approval of all budgetary, financial, policy, and contractual matters. The Board is assisted by an administrative staff and a Citizen Advisory Board.

Each member city is responsible for contributing operating revenues as determined from the ARCH annual budget. Contributions from the member cities are based on each member's population. Contributions by member agencies are held in the ARCH Housing Trust Fund Account and dispersed by the Administering Agency for approved projects. In 2023 the City contributed \$69,646 to ARCH for operations and \$35,000 to fund affordable housing projects which is held in the ARCH Housing Trust Fund. Mercer Islands' accumulated balance in the Trust Fund are considered immaterial and as such are not reflected in the City's cash and cash equivalent balances.

Members withdrawing from the agreement relinquish all rights to any reserve funds, equipment, or material purchased. Upon dissolution, the agreement, as amended, provides for distribution of net position among the members based on the percentage of the total annual contributions during the period of the Agreement paid by each member. The City's share of net position is deemed immaterial and thus is not reflected in the financial statement.

Budget monitoring information can be obtained from ARCH, 16307 NE 83rd Street, Redmond, WA 98052.

NOTE 9 – LEASES

During the year ended December 31, 2022, the City adopted guidance for the presentation and disclosure of leases, as required by the BARS manual. This requirement resulted in the addition of a lease liability reported on the Schedule of Liabilities.

The City leases small equipment that includes copiers and postage machines under lease agreements for 60 and 63 months respectfully. The leases have start dates in 2021 through 2024 and will end in 2024 through 2028.

The City leases building space for the Municipal Court. The current monthly lease amount is \$4,110.50 which includes an 8.03% share of operating costs. The lease began in November 2023 for 38 months with an annual increase of 1% and an annual review and reallocation of operating costs. The current lease period will expire on December 31, 2026.

Due to the permanent closure of City Hall facilities temporary office trailers were leased and installed in support of ongoing Police operations. Leased office trailers and storage units will be located in the existing City Hall parking lot. Monthly rental costs range from \$150 to \$3,700 per month depending on the size and function of modular space. Terms range from 12 to 24 months and are expected to be renewed. Additional details available on the Schedule of Liabilities.

The total amount paid for leases in 2023 was \$76,575. As of December 31, 2023, the future lease payments are as follows:

Year Ending December 31	Total
2024	\$ 297,276
2025	285,638
2026	110,927
2027	1,348
2028	-
2029-2033	0
Total	\$ 695,189

NOTE 10 – LONG TERM DEBT

The accompanying Schedule of Liabilities provides more details of the outstanding debt and liabilities of the City and summarized the debt transactions for the year ended December 31, 2023

The debt service requirements for general obligation bonds, capital financing agreements and Public Works Trust Fund loans are as follows:

Year Ending December 31,	Principal	Interest	Total
2024	\$ 1,143,454	\$ 139,362	\$ 1,282,815
2025	1,124,722	109,030	\$ 1,233,752
2026	1,157,818	78,520	\$ 1,236,338
2027	773,267	58,488	\$ 831,755
2028	695,000	39,375	\$ 734,375
2029-2033	815,000	26,900	\$ 841,900
Total	\$5,709,261	\$451,675	\$ 6,160,936

NOTE 11 – PAID FAMILY MEDICAL LEAVE ACT SELF INSURANCE

The City of Mercer Island administers a voluntary plan for paid family and medical leave benefits for its employees. Voluntary plans are approved by the Employment Security Department and are available for employers who wish to opt out of the State of Washington’s Paid Family & Medical Leave Program for either family leave benefit, medical leave benefit, or both, and instead administer their own internal plan. Employers with voluntary plans are required to offer benefits that are equal to or exceed the benefits offered by the State’s program and must report employee hours, wages, premiums deducted from employee pay, and other information to the Employment Security Department on a quarterly basis.

The City paid \$42,991 in claims during 2023 and held \$0 of employee premiums at year end.

NOTE 12 – PROPERTY TAX

The county treasurer acts as an agent to collect property tax levied in the county for all taxing authorities. Collections are distributed after the end of each month. Property tax revenues are recognized when cash is received by the City. Delinquent taxes are considered fully collectible because a lien affixes to the property after tax is levied.

For 2023 the City's tax levy was \$0.65137 per \$1,000 on a total assessed valuation of \$22,408,435,338 for a total levy of \$14,596,210. Of the total levy for 2023, \$14,382,311 or 98.5% was collected in the current year.

The total property tax levy includes the regular statutory levy and special levies as detailed below:

General Levy	
Regular Statutory Levy	\$ 12,966,888
LID Lifts	
Lid Lift - 2022	1,629,322
<hr/>	
Total Property Tax Levy 2023	<u>\$ 14,596,210</u>

NOTE 13 – RISK MANAGEMENT

The City of Mercer Island is a member of the Washington Cities Insurance Authority (WCIA). Utilizing Chapter 48.62 RCW (self-insurance regulation) and Chapter 39.34 RCW (Interlocal Cooperation Act), nine cities originally formed WCIA on January 1, 1981. WCIA was created for the purpose of providing a pooling mechanism for jointly purchasing insurance, jointly self-insuring, and / or jointly contracting for risk management services. WCIA has a total of 169 members.

New members initially contract for a three-year term, and thereafter automatically renew on an annual basis. A one-year withdrawal notice is required before membership can be terminated. Termination does not relieve a former member from its unresolved loss history incurred during membership.

Liability coverage is written on an occurrence basis, without deductibles. Coverage includes general, automobile, police, errors or omissions, stop gap, employment practices, prior wrongful acts, and employee benefits liability. Limits are \$4 million per occurrence in the self-insured layer, and \$16 million in limits above the self-insured layer is provided by reinsurance. Total limits are \$20 million per occurrence subject to aggregates and sublimits. The Board of Directors determines the limits and terms of coverage annually.

All Members are provided a separate cyber risk policy and premises pollution liability coverage group purchased by WCIA. The cyber risk policy provides coverage and separate limits for security & privacy, event management, and cyber extortion, with limits up to \$1 million and subject to member deductibles, sublimits, and a \$5 million pool aggregate. Premises pollution liability provides Members with a \$2 million incident limit and \$10 million pool aggregate subject to a \$100,000 per incident Member deductible.

Insurance for property, automobile physical damage, fidelity, inland marine, and equipment breakdown coverage are purchased on a group basis. Various deductibles apply by type of coverage. Property coverage is self-funded from the members' deductible to \$1,000,000, for all perils other than flood and earthquake, and insured above that to \$400 million per occurrence subject to aggregates and sublimits. Automobile physical damage coverage is self-funded from the members' deductible to \$250,000 and insured above that to \$100 million per occurrence subject to aggregates and sublimits.

In-house services include risk management consultation, loss control field services, and claims and litigation administration. WCIA contracts for certain claims investigations, consultants for personnel and land use issues, insurance brokerage, actuarial, and lobbyist services.

WCIA is fully funded by its members, who make annual assessments on a prospectively rated basis, as determined by an outside, independent actuary. The assessment covers loss, loss adjustment, reinsurance and other administrative expenses. As outlined in the interlocal, WCIA retains the right to additionally assess the membership for any funding shortfall.

An investment committee, using investment brokers, produces additional revenue by investment of WCIA's assets in financial instruments which comply with all State guidelines.

A Board of Directors governs WCIA, which is comprised of one designated representative from each member. The Board elects an Executive Committee and appoints a Treasurer to provide general policy direction for the organization. The WCIA Executive Director reports to the Executive Committee and is responsible for conducting the day-to-day operations of WCIA.

NOTE 14 – PENSION PLANS

A. State Sponsored Pension Plans

Substantially all the City of Mercer Islands full-time and qualifying part-time employees participate in the following statewide retirement systems administered by the Washington State Department of Retirement Systems (DRS), under cost-sharing, multiple-employer public employee defined benefit and defined contribution retirement plans.

- Public Employees’ Retirement System (PERS)
- Public Safety Employees’ Retirement System (PSERS)
- Law Enforcement Officers’ and Firefighters Retirement System (LEOFF)

The State Legislature establishes, and amends, laws pertaining to the creation and administration of all public retirement systems.

The Department of Retirement Systems, a department within the primary government of the State of Washington, issues a publicly available Annual Comprehensive Financial Report (ACFR) that includes financial statements and required supplementary information for each plan. The DRS ACFR may be downloaded from the DRS website at www.drs.wa.gov.

At June 30, 2023 the City’s proportionate share of the collective net pension liability/(asset) was as follows:

Pension Plan	Employer		Liability / (Asset)
	Contribution	Allocation %	
PERS 1	557,566	0.081823%	\$ 1,867,800
PERS 2/3	922,589	0.104933%	(4,300,871)
PSERS 2	5,850	0.011618%	(12,320)
LEOFF 1	-	0.074490%	(2,210,881)
LEOFF 2	482,392	0.213716%	(5,126,188)

Only the net pension liabilities are reported on the Schedule of Liabilities.

LEOFF Plan 1

The City also participates in LEOFF Plan 1. The LEOFF Plan 1 is fully funded and no further employer contributions have been required since June 2000. If the plan becomes underfunded, funding of the remaining liability will require new legislation. Starting on July 1, 2000, employers and employees contribute zero percent.

LEOFF Plan 2

The City also participates in the LEOFF Plan 2. The Legislature, by means of a special funding arrangement, appropriates money from the state general fund to supplement the current service liability and fund the prior service costs of Plan 2 in accordance with the recommendations of the Pension Funding Council and the LEOFF Plan 2 Retirement Board. This special funding situation is not mandated by the state constitution and could be changed by statute.

B. Local Government Pension Plans

In addition to the two statewide retirement systems, the City is the administrator of a Firefighters Pension Plan. The Firefighters Pension Plan (FPP) is a closed, single-employer defined benefit pension plan established in conformance with Revised Code of Washington (RCW) 41.18. The Plan provided retirement and disability benefits, annual cost of living adjustments, and death benefits to Plan members and beneficiaries. Retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Membership is limited to firefighters employed prior to March 1, 1970, when the LEOFF retirement system was established. The City's obligation under the Plan consists of paying the difference between pension and medical benefits provided by LEOFF1 and those provided by the FPP for covered firefighters who retire after March 1, 1970. At December 31, 2023, there were a total of five individuals covered by this system, five of whom are retired and all of whom qualified to receive benefits during 2023.

Under State law, the FPP is provided an allocation of 25% of all moneys received by the State from taxes on fire insurance premiums. Other funding sources include interest earnings, member contributions made prior to the inception of LEOFF, property taxes committed by action of the City Council, and City contributions required to meet projected future pensions obligations.

The Valuation Date is January 1, 2022. This is the date as of which the actuarial valuation is performed. The Measurement Date is December 31, 2023. This is the date as of which the Net Pension Liability under GASB 67 and 68 is determined. The Reporting Date is December 31, 2023. This is the Plan's and/or employer's fiscal year ending date. As of December 31, 2023, the net pension liability was \$1,669,633 as reported on the Schedule of Liabilities.

NOTE 15 – OTHER POST EMPLOYMENT BENEFITS

In accordance with RCW 41.26, which establishes the Washington Law Enforcement Officers' and Firefighters Retirement System, the city provides lifetime medical care for law enforcement officers and fire fighters employed prior to October 1, 1977. Under this requirement, most coverage for eligible retirees is provided in one of the city's medical insurance programs. However, under authorization of the Disability Board, direct payment is also made for some retiree medical expenses not covered by standard benefit plan provisions. The retiree does not contribute towards the cost of medical care.

The City of Mercer Island's LEOFF Plan 1 (the Health Plan) is a single employer defined benefit healthcare plan administered by the city. The Health Plan provides medical, prescription drug, Medicare premiums, long-term care, and other eligible medical expenses for LEOFF Plan 1 retirees. The Health Plan is closed to new entrants, and dependent spouses and children are not covered. The Plan does not issue a separate standalone financial report.

The Health Plan is funded on a pay-as-you go basis and there are no assets accumulated in a qualifying trust. For the year ending December 31, 2023, there were zero active plan members, 25 retired plan members and the City's cost for providing the benefits was \$343,331.

The Valuation Date is January 1, 2022. This is the date as of which the actuarial valuation is performed. The Measurement Date is December 31, 2023. The Total OPEB Liability was determined by an actuarial valuation as of the valuation date, calculated based on the discount rates of 3.75% and 3.25% respectively, and then projected to the measurement dates.

At December 31, 2023 the total OPEB Liability as determined by an actuarial valuation was \$9,949,584 and is included on the Schedule of Liabilities.

NOTE 16 – SUBSCRIPTION BASED INFORMATION TECHNOLOGY ARRANGEMENTS (SBITA)

During the year ended December 31, 2023, the City of Mercer Island adopted guidance for the presentation and disclosure of Subscription Based Information Technology Arrangements (SBITA), as required by the BARS manual. This requirement resulted in the addition of a subscription liability reported on the Schedule of Liabilities.

The City makes subscription payments of \$833.33 per month for payroll and human resource software optimization. The SBITA contract is for 24 months and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$125 per month for Municipal Court audio services. The SBITA contract is for 36 months and includes an automatic renewal for an additional 36 months.

The City makes subscription payments of \$1,195 per year for codification of the municipal code online. The SBITA contract is for three years and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$14,442.75 per year for Civic Plus software in support of the recreation division. The SBITA contract is for two years and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$70.83 per month for online policy and procedures. The SBITA contract is for 36 months ending in the first quarter of 2024 and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$1,500 per year for hosting the Sister City website. The SBITA contract is for two years and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$30,978.48 per year for cybersecurity. The SBITA contract is for four years and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$8,560 per year for social engagement software. The annual payment escalates each year. The SBITA contract is for three years and includes the option to extend the contract annually after the initial term.

The City makes subscription payments of \$9,000 per year for human resource candidate screening. The SBITA contract is for three years and includes the option to extend the contract annually after the initial term.

The City makes subscription payments for legal research software. In 2023 the monthly payments were \$330 for two months and \$344 for the remaining 10 months. The SBITA contract is for 36 months and includes an annual escalator.

The City makes subscription payments of \$12,725 per year for automated license plate reader software for police vehicles. The SBITA contract is for three years and ending in 2024.

The City makes subscription payments of \$30,000 per year for recreation and facility booking software. The SBITA contract was for three years and has been renewed for an additional three years at \$34,500 per year ending in 2026.

The City makes subscription payments of \$30,500 per year for geographical information software. The SBITA contract is for three years and ending in 2023.

The City makes authorized subscription payments starting at \$27,550 per year, with annual CPI escalation, for automated meter infrastructure software. The SBITA contract is for twenty years beginning when the meter installation project is complete, anticipated in 2024.

The total amount paid for SBITAs in 2023 was \$155,351. As of December 31, 2023, the future SBITA payments are as follows:

Year Ending December 31:	Total
2024	\$ 133,518
2025	116,179
2026	97,496
2027	32,933
2028	32,604
2029-2033	177,414
2034-2038	207,600
2039-2043	240,586
Total \$	1,038,330

NOTE 17 – SUBSEQUENT EVENTS

On October 24, 2024, the City issued \$26,615,000 in Limited Tax General Obligation and Refunding Bonds for the purpose of financing and/or reimbursing the costs of acquiring, designing, constructing, developing, improving, and equipping facilities for City operations, including the City’s water distribution system and refunding current outstanding LTGO Bonds, 2011. Future debt service on the bonds will be paid from the Water Utility.

**City of Mercer Island
Schedule of Liabilities
For the Year Ended December 31, 2023**

ID. No.	Description	Due Date	Beginning Balance	Additions	Reductions	Ending Balance
General Obligation Debt/Liabilities						
251.11	2011 LTGO FIRST HILL WATER IMPROVEMENTS	12/1/2030	735,000	-	80,000	655,000
251.11	2013 REFUNDING CCMV CONSTRUCTION	12/1/2023	140,000	-	140,000	-
251.11	2017 REFUNDING SEWER LAKE LINE	12/1/2029	3,960,000	-	510,000	3,450,000
263.51	2015 MINI PUMPER	6/1/2024	82,420	-	40,699	41,721
263.51	2018 PIERCE ENFORCER	4/9/2027	435,357	-	81,089	354,268
263.56	EQUIPMENT LEASES		135,552	-	49,560	85,992
263.56	FACILITY LEASES		-	636,212	27,015	609,197
263.56	SBITA LIABILITY		1,193,681	-	155,351	1,038,330
263.83	SETTLEMENT DUE TO SOUND TRANSIT	12/31/2024	2,100,000	-	575,000	1,525,000
Total General Obligation Debt/Liabilities:			8,782,010	636,212	1,658,714	7,759,508
Revenue and Other (non G.O.) Debt/Liabilities						
259.12	TOTAL COMPENSTATED ABSENCE LIABILTY		1,868,809	-	242,720	1,626,089
259.12	DUE TO EASTSIDE FIRE AND RESCUE		-	1,109,615	-	1,109,615
263.93	ARO WATER WELL		92,000	-	-	92,000
264.30	PENSION LIABLITY		2,735,735	801,698	-	3,537,433
264.40	LEOFF 1 OPEB		9,496,481	453,103	-	9,949,584
263.88	PWTF SEWER LAKE LINE	7/1/2026	1,611,030	-	402,757	1,208,273
Total Revenue and Other (non G.O.) Debt/Liabilities:			15,804,055	2,364,416	645,477	17,522,994
Total Liabilities:			24,586,065	3,000,628	2,304,191	25,282,502

ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the Washington State Constitution and is part of the executive branch of state government. The State Auditor is elected by the people of Washington and serves four-year terms.

We work with state agencies, local governments and the public to achieve our vision of increasing trust in government by helping governments work better and deliver higher value.

In fulfilling our mission to provide citizens with independent and transparent examinations of how state and local governments use public funds, we hold ourselves to those same standards by continually improving our audit quality and operational efficiency, and by developing highly engaged and committed employees.

As an agency, the State Auditor's Office has the independence necessary to objectively perform audits, attestation engagements and investigations. Our work is designed to comply with professional standards as well as to satisfy the requirements of federal, state and local laws. The Office also has an extensive quality control program and undergoes regular external peer review to ensure our work meets the highest possible standards of accuracy, objectivity and clarity.

Our audits look at financial information and compliance with federal, state and local laws for all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits and cybersecurity audits of state agencies and local governments, as well as state whistleblower, fraud and citizen hotline investigations.

The results of our work are available to everyone through the more than 2,000 reports we publish each year on our website, www.sao.wa.gov. Additionally, we share regular news and other information via an email subscription service and social media channels.

We take our role as partners in accountability seriously. The Office provides training and technical assistance to governments both directly and through partnerships with other governmental support organizations.

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