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Seattle Department of Transportation Bonds Management Audit

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Seattle Office of City Auditor

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REPORT SUMMARY

Although the City's annual budget process defines the basic steps involved in the planning and issuance of the Seattle Department of Transportation's (SDOT) limited tax general obligation (LTGO) bonds, the City should improve communications between the involved departments and the City Council by clarifying roles and formalizing and improving internal policies and procedures for bond planning and spending of proceeds.

Seattle Department of Transportation Bonds Management Audit

SEATTLE OFFICE OF CITY AUDITOR

Report Highlights

Background

The City of Seattle regularly issues limited tax general obligation (LTGO) bonds to finance portions of the Seattle Department of Transportation's (SDOT) Capital Improvement Program (CIP). In early 2013, the City Council and the City Budget Office (CBO) expressed concern about SDOT's cumulative unspent bond proceeds from LTGO bond issuances dating back to 2008 (e.g., $113.8 million unspent by the end of 2011).

Our Conclusions

The decision about the amount and timing of issuing LTGO debt for the City's CIP involves weighing uncertainties about the City department's CIP spending projections with borrowing uncertainties within the bond market. According to the City Finance Director, in hindsight, during 2008-2011, the City could have better timed issuing bonds for SDOT until the immediate need for funds was certain. However, in doing so, the City would have taken the risk that bond rates would increase.

According to the City's Director of Debt Financing:

1) Most market experts at the time believed that there was a greater risk of bond rates rising than falling, however, bond rates during that period ultimately declined and then remained low much longer than anticipated;
2) Unexpectedly large bond balances resulted from the timing of the City's borrowing relative to actual spending, not from the overall amount of borrowing for its six-year CIP;
3) Since the City would have borrowed about the same amount for these SDOT projects over time regardless of when it incurred the debt, the City's total financing costs are about the same over the long run;
4) If some of the borrowing had been deferred, bond balances would have been smaller, but this would have merely shifted some of the City's annual debt service out into the future; and
5) Interest earned on unspent bond proceeds partially offset annual debt service.

Our office did not perform an analysis to calculate the financial impacts of borrowing more bonds initially over deferring or shifting the borrowing to

WHY WE DID THIS AUDIT

Seattle Councilmember Tim Burgess requested this audit because he was concerned about SDOT's accumulation of unspent LTGO bond proceeds in 2011 and 2012. His concern was about whether the City and SDOT have processes and controls in place to reduce the likelihood of unspent bond fund balances. He also wanted to know whether the City could take steps to avoid such occurrences in the future.

AUDIT SCOPE

We focused our work on 1) City and department-level policies and processes related to determining bond amounts issued to support SDOT's CIP from 2008 through 2012, and 2) inter-departmental communication about bond spending.

about 3 to 5 years later. We focused on determining the cause(s) of SDOT's unspent LTGO bond balances and developing recommendations to help reduce the future likelihood of ongoing bond balances.

When concerns were raised in early 2013 by CBO and City Councilmember Tim Burgess about SDOT's accumulation of 2011 and 2012 unspent bond balances, their concerns could have been diffused by better communication between SDOT, the City Department of Finance and Administrative Services (FAS), CBO, and the City Council to clarify why SDOT was not able to spend its bond proceeds as quickly as planned.

Multiple factors at the national, local, and departmental levels contributed to SDOT's delay in bond spending, which resulted in accumulated unspent bond proceeds between 2008 and 2012.

Factors that contributed to SDOT's unspent bond balances included:

- Changes in project schedules when SDOT could not proceed on certain projects or project tasks until partner agencies completed their portions of the work.
- The City of Seattle had a favorable construction bidding climate between 2007 and 2009, during which it received lower-than-expected bids to complete construction projects.
- In 2008 and 2009, the City Council took several actions outside the annual budget process to fund Bridging the Gap (BTG) transportation projects by increasing SDOT's bond proceeds. This included shifting bond funds originally intended for a parking garage and a jail to SDOT for use on BTG projects.
- SDOT's 2008 and 2009 LTGO bonds were planned to cover two years each instead of one year, so the second year funding was intentionally held for spending in the second year.
- The City's initial decisions on the budget for bond funding are made 6 to 12 months in advance of when the bond funds are available for use. During that period, the department's projected cash needs could change significantly and the City makes corresponding adjustments to the actual amount of bonds to be issued.
- The City's legislative requirements and process for shifting bond funding from planned projects to other SDOT projects can take from 6 to 12 months, slowing the use of bond proceeds.
- Grant funding often takes priority over the spending of bond funds because granting agency spending requirements often carry a condition that the funding be spent immediately. When new grants are added to a project's funding plan, SDOT's practice is to spend grant funding first, because bond funds can be spent later. This can delay the spending of bond funds.
- SDOT's cost projections include funds to cover project assumptions, risks, contingencies, and inflation that help ensure that full funding is in place before issuing contracts for a project or portion of a project. Over the life of a project, these costs may or may not be incurred.
- Because SDOT dedicates contingency amounts for each project and has a practice of retaining all remaining project funds until all costs are identified and potential disputes are resolved, this can increase the amount of bond funds needed and delay their spending.
- Litigation on a project slowed the use of some bond proceeds.
- The City Council sometimes adds funding and bond proceeds to projects during the annual budget process.

Finally, the City's Debt Management Policies were last updated in 2003 and at the time of our audit field work some of them did not reflect the City's current practices for the issuance and management of debt.

Our Recommendations

We made the following 8 recommendations:

1. To facilitate shifting bond funds among different projects when there are excess bond proceeds, the City Council could consider increasing threshold amounts for transfers that require supplemental legislation.
2. SDOT should work with CBO, FAS, and the Law Department to explore changes to SDOT'S CIP structure to enable greater flexibility in moving bond funds among projects. For example, grouping similar projects under one project title in the CIP, as was done with the Bridge Rehabilitation list of Bridging the Gap projects, could provide SDOT with greater flexibility in re-purposing bond funds among its projects.
3. The City should consider basing SDOT's bond needs on less than 100% of the project's estimated one year cash needs by encouraging the use of short-term financing for gap funding (e.g., Interfund loans) if needed, to fund the project until proceeds from the next bond issuance become available. For this approach to work, CBO, FAS, the Mayor, and the City Council would need to support SDOT's use of short-term financing and enable SDOT to obtain it quickly and efficiently. Short-term financing should be considered for projects at their initial stages, when there are many unknowns, until more definitive project cost data is available. This would allow the project's long-term financing to be arranged during a later design phase with greater accuracy.
4. FAS should establish and provide training to City departments on written formal policies and procedures related to the bonds process including delineating roles and responsibilities, planning for bond needs; and managing, tracking and communicating spending of bond proceeds. The procedure for the final check-in between FAS and SDOT before bonds are issued should be included in the formal bond process policies and procedures. The records retention requirements for significant bond process communications should also be delineated in the formal policies and procedures.
5. The Debt Management Policy Advisory Committee (DMPAC) should consider inviting City departments that have bond funding to attend DMPAC meetings to answer questions that might arise about their use of bond funds.
6. If unspent bond balances continue to be a concern of the City Council, CBO and SDOT could provide the Council, during the budget process, with summarized data on unspent bond proceeds by each bond issue, and the reasons for any spending delays.
7. SDOT should Include and track all bond proceeds in bond monitoring reports.
8. The City's Debt Management Policies should be updated to reflect the City's current practices for the issuance and management of debt.

Executive Response

The City Budget Director, City Finance Director, and the City's Director of Debt Financing provided a written response to this audit in which they concurred with our recommendations (Appendix G).

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I. INTRODUCTION

In early 2013 the City Council and the City Budget Office (CBO) expressed concern about unspent bond proceeds[1] from issuances dating back to 2008 that were intended to fund transportation projects for the Seattle Department of Transportation (SDOT). According to SDOT, from 2002 through 2012, the City issued $339 million in limited tax general obligation (LTGO) bonds[2] to finance portions of SDOT's Capital Improvement Program. During this period, the cumulative unspent balance was, at its highest, $113.8 million, at the end of 2011. City Councilmember Tim Burgess asked our office to examine SDOT's management of its bond proceeds and to recommend any needed controls that would reduce the likelihood of future unspent bond balances.

In this report we make eight recommendations. The City Budget Director, City Finance Director, and the City's Director of Debt Financing provided a written response to this audit in which they concurred with our recommendations (Appendix G).

II. BACKGROUND

Limited Tax General Obligation Bonds

The City regularly issues limited tax general obligation (LTGO) bonds to help finance its large capital programs, and a large portion of the bonds issued are for SDOT's CIP. (See Chart 1 for SDOT's LTGO bond history 2002-2013.) LTGO bonds are one type of debt the City uses to finance its capital improvement programs (CIP). [3] LTGO bonds are a type of debt that does not require approval by the voters. The Seattle City Council has the authority to issue LTGO bonds (also known as Councilmanic bonds) up to an amount established by state law (i.e., 1.5 % of assessed value of taxable property), hence the term, "limited". The City pledges its full faith and credit to the payment of principal and interest on LTGO bonds, and the debt must be paid from existing revenue sources such as the General Fund, certain special revenue funds, and reimbursements from proprietary City funds. When the City sells (issues) the LTGO bonds, it promises to repay bond holders the principal with interest (the debt service).

The funding sources to pay the debt service for 2008-2012 LTGO bonds issued for SDOT projects include the following: commercial parking tax revenues, the General Fund, and King County Proposition 2.

Planning for Bond Needs

SDOT uses a combination of funds to pay for its CIP[4]: the 2006 Bridging the Gap levy, other local revenues[5], long-term financing[6] (i.e., LTGO and UTGO[7] bonds), and external funding[8] from grants and

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[1] CBO and FAS became aware of the unspent bond proceeds when CBO looked into re-purposing surplus bond proceeds from the Spokane Street project, which was closing out under budget in early 2013. CBO then discovered that there were unspent bond proceeds from other SDOT projects as well, and confirmed this with FAS.

[2] Limited tax general obligation (LTGO) bonds are one of the types of debt the City uses to finance its capital improvement programs (CIP).

[3] The two other types of debt used to finance the City's CIP are unlimited tax general obligation (UTGO) bonds and revenue bonds.

[4] Source: 2013-2018 Adopted CIP, p. 253

[5] In addition to Bridging the Gap, other local funding sources for the Transportation CIP include the City's General Fund, Gas Tax, Real Estate Excise Tax (REET), the $20 Vehicle License Fee, surplus property sales, a portion of the Commercial Parking Tax, and a property tax levy for the Elliot Bay Seawall (2013-2018 Adopted CIP, p. 253)

[6] Several major projects are partially financed with general obligation bonds. The debt service on these bonds is supported by the Commercial Parking Tax, anticipated local improvement district revenues, and other sources. (2013-2018 Adopted CIP, p. 253)

[7] Unlimited Tax General Obligation bonds are bonds issued after receiving approval by 60% of the voters in an election with at least a 40% turn-out. The debt service on these bonds is repaid from additional ("excess") property tax revenues that voters approve as part of the bond measure. Source: 2013-2018 Adopted CIP, p. 863

partnerships. SDOT projects how the spending of the various funding sources will be spread across the duration of the project. The City's annual budget and the CIP process determines the amount of bonds required as part of a project's funding package.

Project bond needs are based on the department's projected cash needs for the "bond year," (the second quarter of the budget/CIP year through the first quarter of the following year). Ideally, the bond proceeds will be spent over this four-quarter period according to the planned schedule with close to $0 remaining at the end of March of the following year.

The City's Director of Debt Financing stated that he attempts to meet cash-flow needs projected by departments for the "bond year" (i.e., April - March of the following year). Conversely, departments receive budget authority for January 1-December 31, i.e., the "budget year".

While the responsibility for determining the size of the City's bond issuance each year rests ultimately with the City Council, the process for developing a recommendation to the City Council on bond issuances involves CBO, the Mayor's Office, the City's Budget Director, Director of Finance, and Director of Debt Financing, and the Debt Management Advisory Committee (DMPAC).

SDOT proposes how much in LTGO bonds is needed for its upcoming CIP as part of its budget submittal in early July each year. SDOT's proposal is then reviewed by CBO, the City's Director of Debt Financing, DMPAC, and the Mayor. The Mayor's proposed budget is sent to the City Council each September, and the final budget for the following year's bond issuance is included in the City's budget, which is passed by December 1st each year. Bonds are not issued until the late spring each year. In the first quarter of the budget year the City's Director of Debt Financing requests an update on the need for new bond funding from departments budgeted to receive bond funding in the spring bond issuance. The final decision on the amount of bonds actually sold is made by the Mayor and the City Council based on the recommendation of the City's Budget Director, Director of Finance, Director of Debt Financing and DMPAC.

Please see Appendix A for a chart showing an overview of the roles and responsibilities of the entities involved in the City's LTGO bonds process.

Bond Authorization

Together with the adoption of the budget and CIP, the City Council passes a bond ordinance authorizing a maximum bond amount for the next issuance. The bond ordinance contains a list of projects upon which the bond proceeds may be spent and an approximate amount for each project.

Bond Issuance

By the end of the first quarter of the following year, the department should have a more accurate projection of its unspent bond proceeds balance and cash needs for the next bond year. This information allows the City to make adjustments to the amount of new bonds immediately before the bond sale. The City's Director of Debt Financing contacts SDOT before the bond sale to confirm the department's final bond amount.

When bonds are sold, the City Council adopts a resolution authorizing their terms and conditions.

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[8] This category includes partners in regional efforts, such as King County, Sound Transit, the Port of Seattle, and the Washington State Department of Transportation, and funding from the city's utilities for utility relocations and betterments in association with transportation projects. (2013-2018 Adopted CIP, p. 253)

Spending Bond Proceeds
Bond proceeds are available to SDOT typically in the spring of each year, soon after the bonds have been issued. According to the City's Director of Debt Financing, a department should have planned its cash needs over each bond year and should try to have completely spent the bond proceeds by the end of the bond year. However, unexpected situations can occur that accelerate or slow down the spending of proceeds.

For example, schedule delays will slow spending, but SDOT "carries-over" the amounts to the following year because the project is ongoing. Similarly, lower-than-anticipated construction bids can result in unspent bond proceeds.

Re-purposing Bond Proceeds
SDOT can, with certain restrictions, re-purpose bond funds by moving the funds to another project via a "budget transfer" or "budget revision." Bond proceeds are tied to specific SDOT projects, so, typically, unspent bond proceeds are carried over for use on the specified project the following year. SDOT re-purposes unspent bond funds if they know that they will not need the proceeds, typically at the end of a project, or if there is a significant delay of a year or more in using the funds for a particular project. In such cases, bond proceeds may be moved to other CIP projects but the funds must be appropriated according to the City's budget revision and transfer rules. Federal and state rules for municipal bonds may also affect SDOT's ability to repurpose bond proceeds.

SDOT's LTGO Bond History
According to SDOT, between 2002 and 2012 the City issued $339[9] million in LTGO bonds to finance SDOT's CIP; no LTGO bonds were issued for SDOT in 2013.

Chart 1: SDOT LTGO Bond History 2002-2013

Bond Issuance Year	Amount	Spending period covered
2002	$2,100,000	2 years
2003	$2,860,000	1year
2004	$0	
2005	$21,764,000	3 years[10]
2006	$7,720,000	1 year
2007	$22,620,000	1 year
2008	$65,187,202	2 year
2009	$64,350,877	2 year
2010	$74,636,324	1 year
2011	$61,686,588	1 year
2012	$15,935,000	1 year
2013	$0	

Source: SDOT[11]

[9] $338,859,991 (these are SDOT's #s from 2014 monitoring spreadsheet)
[10] According to SDOT staff, their projection for spending the bond funds dedicated to the parking pay stations was over three years.
[11] Source: 2013 LTGO Bond Monitoring Report Year End 2013.xlsx; Tab: SDOT Bond History 2002-2013

SDOT's Unspent Bond Balances

The following chart shows our compilation of SDOT's cumulative unused 2008-2012 bond balances at the end of each calendar year.[12]

Chart 2: SDOT's Cumulative Unused 2008-2012 Bond Balances ($)							
Bond Issue	Beginning Balance	Q4 2008	Q4 2009	Q4 2010	Q4 2011	Q4 2012	Q4 2013
2008	65,187,202	48,936,203	20,047,449	11,945,185	9,945,361	6,952,246	212,813
2009	64,350,877		40,428,717	30,177,916	12,236,029	609,292	406,477
2010	74,636,324			51,133,207	36,349,551	8,139,427	4,218,322
2011	61,686,588				55,250,843	38,808,519	12,402,352
2012	15,935,000					10,800,000	7,094,304
Cumulative		48,936,203	60,476,166	93,256,308	113,781,784	65,309,484	24,334,268

Source: SDOT

CBO Analysis of SDOT's Unspent Bond Balance

In March 2013, CBO produced a report[13] based on SDOT information that reviewed SDOT's bond spending patterns between 2009 and 2012 (See Appendix B). SDOT identified seven reasons why bond spending was delayed for bonds issued in 2009-2012, and the CBO report showed the percentage of accumulated bond funds resulting from each reason as follows:

1. Shifts in project schedules (47%)
2. Availability of grants or other outside funding (14%)
3. Lower bids due to recession (13%)
4. Refined cost assumptions (11%)
5. Bond issuances that were intended to cover a two-year period, e.g., 2009 (8%)
6. Contingencies not needed to the extent originally assumed (4%)
7. Other miscellaneous reasons such as litigation or City Council actions (3%)

The CBO report also discussed steps taken to date to address the unspent bond proceeds, and additional steps CBO and FAS were planning to implement.

III. OBJECTIVES, SCOPE, AND METHODOLOGY

Objectives

We conducted this performance audit of the Seattle Department of Transportation's (SDOT) management of LTGO bonds at the request of City Councilmember Tim Burgess. The specific audit objectives were to:

1) Determine the cause(s) of SDOT's unspent LTGO bond balances in 2010 and 2011; and
2) Develop recommendations to help reduce the future likelihood of ongoing bond balances.

Scope and Methodology

We focused our work on the management of LTGO bonds issued from 2008 through 2012 by the City of Seattle for the SDOT capital improvement program (CIP). To accomplish the objectives, we did the following:

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[12] These are SDOT's reported cumulative balances on an accrual basis, not cash balances, at the end of each year. The balances shown account for expenses (i.e., liabilities) incurred but not yet paid.

[13] "Analysis of SDOT's Spending Patterns on LTGO Bond Proceeds" See Appendix B.

1. Interviewed officials from SDOT, FAS, CBO, Seattle City Council Central Staff, the Law Department, the Seattle City Council Transportation Committee chair and staff to the City Council Transportation Committee
2. Reviewed and analyzed
    a. City ordinances and laws
    b. Applicable City debt and financial policies
    c. Applicable City Council briefings
    d. "Final Numbers" documents prepared by the City's financial advisor[14]
    e. SDOT, CBO, and FAS documents and spreadsheets on bond history, spending, and carrying costs
3. Performed queries on bond account balances in Summit (the City's financial system)
4. Attended three Debt Management Policy Advisory Committee meetings

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives, except that we did not test the reliability of the computer-generated data that we received from City departments.

IV. CONCLUSIONS AND RECOMMENDATIONS

This section describes in detail the following conclusions along with our recommendations for improvement.

Conclusion 1:
When concerns were raised in early 2013 by CBO and City Councilmember Tim Burgess about SDOT's accumulation of 2011 and 2012 unspent bond balances, poor communication between SDOT, FAS, CBO, and the City Council meant that there were not clear responses made to address the concerns. Better communication between SDOT, FAS, CBO, and the City Council to clarify why SDOT was not able to spend its bond proceeds as quickly as planned could have diffused the concerns.

Each summer as part of the City's budget process, SDOT develops and submits its project funding plans to CBO so that CBO, the Mayor's Office, FAS and DMPAC can review and finalize them for the Mayor's proposed budget and CIP. The request for bond funds is a significant part of the funding plans detailed in each year's CIP. The decision about the amount and timing of issuing LTGO debt for the City's CIP, involves weighing uncertainties about the City department's CIP spending projections[15] and uncertainties within the bond market.

According to the City Finance Director, in hindsight, during 2008-2011, the City could have better timed issuing bonds for SDOT until the immediate need for funds was certain. However, in doing so, the City would have taken the risk that bond rates would increase.

According to the City's Director of Debt Financing, most market experts at the time believed that there was a greater risk of bond rates rising than falling. However, bond rates during that period ultimately declined and then remained low much longer than anticipated.

[14] These are documents, entitled "Final Numbers", prepared by the City's financial advisor, which is a record of the proceeds and structure of each bond issue.
[15] See Appendix C, Chart 4 which compares SDOT's projected to actual spending of 2008-2012 bond proceeds.

He explained further that unexpectedly large bond balances resulted from the timing of the City's borrowing relative to actual spending, not from the overall amount of borrowing for its six-year CIP. Since the City would have eventually borrowed about the same amount for these SDOT projects regardless of when it incurred the debt, he stated that the City's total financing costs are about the same over the long run; if some of the borrowing had been deferred, bond balances would have been smaller, but this would have merely shifted some of the City's annual debt service out into the future. In the short-run, unspent bond proceeds earned interest, partially offsetting annual debt service.

According to the City's Director of Debt Financing:

> In determining how much of its capital program to debt finance each year, the City must balance numerous complex factors including uncertainty about spending projections across multiple departments and projects, uncertainty about dynamic market conditions, the City's legislative and budget schedules, and transaction costs. Within the context of this uncertainty, accumulated bond balances resulted not from decisions about how much the City should borrow for its six-year capital program, but rather from the *timing* of that borrowing relative to actual spending. Even if SDOT's spending projections had been perfect, the City still would have issued about the same amount of debt over time. In hindsight, it is clear that spending occurred more slowly than predicted and that the issuance of some of the debt during the 2008-2012 study time period could have been deferred. But this would have simply shifted annual debt service out into the future and the City's total financing costs would have been about the same over the long-run, all else being equal. In the short-term, unspent bond proceeds earned interest, that partially offset annual debt service.
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> Also, when determining how much debt to issue each year the City must also consider uncertainty about market conditions. During the study period, interest rates were unusually low and most experts predicted that interest rates were more likely to rise than to fall. As such, there was an inherent risk that a deferral of borrowing would result in much higher long-term borrowing costs over the life of the debt. Had the City deferred more of its borrowing and market experts had been correct, the City would have a debt portfolio today bearing higher interest rates and much higher long-term debt service costs. As it turned out, market rates remained low longer than most experts anticipated.

In summary, as explained by the Director of Debt Financing:

1) Most market experts at the time believed that there was a greater risk of bond rates rising than falling, however, bond rates during that period ultimately declined and then remained low much longer than anticipated;
2) Unexpectedly large bond balances resulted from the timing of the City's borrowing relative to actual spending, not from the overall amount of borrowing for its six-year CIP;
3) Since the City would have eventually borrowed about the same amount for these SDOT projects regardless of when it incurred the debt, the City's total financing costs are about the same over the long run;
4) If some of the borrowing had been deferred, bond balances would have been smaller, but this would have merely shifted some of the City's annual debt service out into the future; and
5) In the short-run, unspent bond proceeds earned interest, partially offsetting annual debt service.

Our office did not perform an analysis to calculate the financial impacts of borrowing more bonds initially over deferring or shifting the borrowing to about 3 to 5 years later. This audit focused on determining the cause(s) of SDOT's unspent LTGO bond balances in 2010 and 2011, and developing recommendations to help reduce the future likelihood of ongoing bond balances.

When concerns were raised in early 2013 by CBO and City Councilmember Tim Burgess about SDOT's accumulation of 2011 and 2012 unspent bond balances, better communication between SDOT, FAS, CBO, and the City Council to clarify why SDOT was not able to spend its bond proceeds as quickly as planned could have diffused the concerns.

Conclusion 2:
Multiple factors contributed to SDOT's delays in bond spending, which resulted in accumulated unspent bond proceeds between 2008 and 2012.

A combination of factors at national, City, and department levels contributed to SDOT's delay in bond spending and resultant unspent bond proceeds between 2008 and 2012[16].

Factor 1: CBO's 2013 paper discusses that the largest percentage of bond proceed balances accumulated between 2009 and 2012 is the result of changes in project schedules, accounting for 47 percent of the unspent cumulative balance. Many of these changes in project schedules were because SDOT's work was dependent on partner agencies, e.g., Washington State Department of Transportation, completing their portions of the work. The CBO report states the following:

> Because shifts in project schedules can happen on a project over multiple years, the prevalence of this variable in driving unused bond proceed amounts can happen with a greater frequency than the other variables described in this analysis. For example, in 2010, $6.3 million in bonds issued that year for the Spokane Street Viaduct project were not spent in 2010 due to a delay in obtaining approvals from WSDOT to construct the eastern-most section of the bridge. As a result, SDOT could [not] advertise the project for bids, which then caused additional delays on spending the proceeds in 2011 and 2012. By the end of 2012, $603,000 of these bond proceeds had not been spent as a result of the 2010 delay in obtaining permits from WSDOT. To demonstrate how this plays out over the life of this analysis, SDOT accumulated …$61.7 million of unused bond proceeds over the period between 2009 and 2012 as a result of schedule shifts related to WSDOT and other variables. This $61.7 million does not represent savings as most of the funds were simply spent at a later time. The net savings at the end of the Spokane Street project is approximately $14 million.

Factor 2: Favorable bidding climate.
CBO's 2013 paper, "Analysis of SDOT's Spending Patterns on LTGO Bond Proceeds", identified lower bids due to the 2009 Great Recession as a factor that delayed bond spending. The CBO report states:

> The third most common factor driving the build-up of bonds proceeds, accounting for 13% of the accumulated proceeds over the period 2009 through 2012, is SDOT receiving lower-than-anticipated bids from outside vendors. At the height of the economic downturn, SDOT benefited greatly from a number of bids coming in lower than anticipated. In fact, 26% of the proceeds not needed in 2010 were the result of bids coming in lower than anticipated. This resulted in savings in a number of projects, including the Bridge Rehabilitation and Replacement Program. For example, it cost the City $19.2 million less to replace the 45th Street Viaduct structure as a result

[16] Our conclusions mirror some of the conclusions of CBO's 2013 report, "Analysis of SDOT's Spending Patterns on LTGO Bond Proceeds", (attached as Appendix B), and we include and attribute CBO's conclusions as applicable.

of the contractor providing an alternate design and construction method. As a result, SDOT needed less bond proceeds than originally anticipated when the bonds were issued.

Factor 3: In 2008 and 2009, the City Council took several actions outside the annual budget process to fund Bridging the Gap (BTG) transportation projects by increasing SDOT's bond proceeds. This included shifting bond funds originally intended for a parking garage and a jail to SDOT for use on BTG transportation projects.

In November 2006, voters in Seattle passed the $365 million Bridging the Gap (BTG) levy to fund numerous transportation maintenance and safety projects, including road and bridge repairs, and several major projects such as the Spokane Street Viaduct and Mercer Corridor improvements. At the outset BTG was to be funded by revenues from the Levy LID Lift, the Commercial Parking Tax, and Employee Business Tax. However, since these revenues come in gradually over many years, City decision makers decided to use the City's cash pool[17] and bond funding to accelerate spending on BTG[18] projects so that the projects, which would require large cash outlays for construction, would not have to be delayed waiting for revenue from these taxes but could be started right away. Also, according to an SDOT official, many of these projects needed to be completed before the demolition of the Alaskan Way Viaduct, originally planned for 2012.

In 2008 and 2009 City decision makers took several actions outside the annual budget process to fund BTG projects by increasing SDOT's bond proceeds.

- In 2008[19], via Ordinance 122696 (May 2008), the City 1) added $55.9 million[20] to SDOT's original 2008 bond request, and 2) re-purposed $16.3 million of 2007 bonds from the Zoo Garage to the Mercer Corridor project. The total resulting increase in 2007 and 2008 bonds to SDOT was $72.2 million. At the time, there was a favorable economic climate for the City to issue bonds to cover more than one bond year.[21]
- In November 2009[22], (after the 2009 bonds were issued), Ordinance 123156 increased SDOT's 2009 bonds from $64.7 million to $68.8 million by re-purposing $4.1 from the Jail project to the Spokane Street Viaduct.

The Mercer and Spokane projects did not need the bond funds as quickly as anticipated by City decision makers and SDOT carried over the bond funds to be spent later because:

- The projects were still in their design stages;
- The City needed to coordinate with the Washington State Department of Transportation on the Spokane Viaduct;
- The increase to Mercer was originally intended for right-of-way purchases that were instead accomplished through property swaps that did not require an outlay of all the City dollars, and the funds were then re-purposed to the construction phase; and

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[17] In the whereas clauses of Ordinance 122417.
[18] Ordinance 122417.
[19] The City via Ordinance 122696 (May 2008) increased SDOT's bonds for 2008 from $13,034,650 to $68,933,105, an increase of $55,898,455, all to BTG projects. Specific amounts of increase per project included: Spokane ($9,270,000), Mercer ($43,439,575), South Lander St ($2,833,530); and King Street Station $(355,350). Ordinance 122696 also re-purposed $16,300,000 of 2007 bonds from the Zoo Garage to the Mercer. Total resulting increase in 2007 and 2008 bonds to SDOT was $72,198,455
[20] The original 2008 bond ordinance authorized up to$13 million for SDOT.
[21] 2008 and 2009 bond issuances were intended to each cover two years of CIP spending.
[22] In Nov 2009 (after the 2009 bonds were issued), Ordinance 123156 increased SDOT's 2009 bonds from $64,646,452 to $68,773,037 by re-purposing $4,126,585 from the Jail project to the Spokane Street Viaduct.

- In lieu of bond funds the City spent $15.4 million in American Recovery and Reinvestment Act (ARRA) grant funds for the Spokane Viaduct.

Factor 4: The LTGO bonds for 2008 and 2009 were planned to cover cash flow needs for two years each, so some spending was always assumed to occur in the second year.

Between 2002 and 2009, many of the City's bond issuances were intended to cover multiple years' worth of cash flow needs. Normally, SDOT annually updates its spending plan to request appropriation authority for costs anticipated in the budget year, but when bonds are issued to cover spending for two years, this update does not occur.

SDOT gave us an example from the 2008 budget process, during which they estimated that for the Mercer East project, SDOT would need bonds for $3.241 million in 2008 and $38.933 million in 2009. Although their appropriation amount was $3.241 million in 2008, $42.3 million for the project was issued in 2008, "locking them" into the 2009 amount without an opportunity to adjust it downward in the next budget year

Multi-year bonds may have been issued in the past to take advantage of a favorable bond issuance climate.

The City shifted in recent years[23] to borrowing for one year at a time rather than borrowing to cover multiple years, and this makes it easier to more accurately adjust the borrowing amount.

Multi-year bond sales were also identified in CBO's 2013 paper as a factor which delayed bond spending. The CBO report states:

> The City had an earlier practice of issuing bonds to cover two-year's worth of cash flow needs as a strategy for taking advantage of relatively strong investment rates. This practice was in place with the 2009 bond sale. Of the $64.4 million in bonds issued in 2009, $22.9 million was intended to cover cash flow needs in 2010 – mostly in the first quarter. This practice in 2009 accounts for 8% of the unused bond proceeds accumulated over the period 2009-2012.

Factor 5: Initial estimates on the budget for bond funding are made 6 to 12 months in advance of when the bond funds are available for use. During that period, the department's projected cash needs could change significantly and the City makes corresponding adjustments to the actual amount of bonds to be issued.

Bond fund needs are initially communicated by SDOT to CBO and FAS through the budget process about 6 to 12 months in advance of the time when departments receive bond funds and start spending the proceeds. SDOT's accuracy in estimating project cost and schedules depends on information available at the time these numbers are developed and the project phase when the estimate is provided. Projects in their early stages have many unknowns, so a higher level of contingency is factored into the project cost in accordance with industry standards.

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[23] In order for the City to shift to appropriating on a year-to-year basis and still be compliant with state law, the City Council passed Ordinance 123746 in November 2011. The ordinance stated that for contracts spanning multiple years (i.e., construction contracts, leases, etc.), the City department still needs to certify that full funding for the contract amount has been appropriated for the budget year and allocated in the 6 year CIP. A "Termination for Convenience" provision is included in the contract, allowing the City to terminate the contract for convenience without liability.)

Because of the time lag, cash needs that were projected based on known factors and assumptions during the budget planning period may change by the time the department receives the bond funds. For example, the project may have been delayed, or grant funds may have been received. In both cases, spending of bond funds could be delayed.

The uncertainties of construction projects contribute to the change in need for funds. During the planning process, there are many opportunities to make adjustments to the actual amount of bonds to be issued, as SDOT projections are refined. The City's Director of Debt Financing stated he has had a longstanding practice of checking with departments in the months immediately before a bond issuance to request adjustments to the bond amount stated in the budget in order to increase its accuracy. Depending on the project's design level at the time an estimate is provided, there could still be substantial changes in the need for bond funds from the time of the initial budget estimate to the time of bond issuance.

According to CBO's 2013 paper:

> Approximately 11% of the bond proceeds accumulated between 2009 and 2012 is the result of refined cost assumptions. It is important to understand that cost assumptions for a project – particularly larger projects – are refined and subject to change over time. A cost estimate used to build the adopted budget is typically developed many months before the project actually commences. In that period of time, SDOT is continually refining and fine-tuning its cost assumptions. Most of the refined cost assumptions related to SDOT's bridge rehabilitation and seismic programs where SDOT was completing several different bridge projects in tandem (e.g., East Duwamish, 15th Ave NE, Jose Rizal, Airport over Argo, NE 45th Street). As a result of cost savings and the receipt of a $4.6 million federal grant, SDOT was able to begin design on two additional bridges, Fairview and Yesler. Spending plans and cost estimates were adjusted accordingly.

Factor 6: The re-purposing of SDOT bond funds is slowed by the City's process for shifting funds to other projects.

The City's legislative requirements and process for shifting bond funding from planned projects to other SDOT projects, i.e., re-purposing funds, can take from 6 to 12 months, slowing the use of bond proceeds. Without supplemental legislation, SDOT can generally transfer up to $500,000 between CIP projects across Budget Control Levels and up to $999,999 within a Budget Control Level. (Both limits are cumulative transfers against all projects for the calendar year.) Otherwise, supplemental legislation is required, which slows the shifting of unused bond funds to other projects.

Process and Considerations for Re-purposing Bond Funds
Please see Appendix D for a discussion of 1) the bonds re-purposing process, and 2) considerations for re-purposing bonds that require legislation.

Time Needed For Re-purposing Bond Funds
If the re-purposing of bond funds requires an amendment to the budget legislation and/or the bond issuance legislation, it generally takes several months to develop the legislation and take it through the City's process for reviewing and passing legislation. If the re-purposing is part of the Supplemental Budget Legislation, according to SDOT, it can take up to seven months for the process to be completed, including internal SDOT discussions to re-purpose, notifying CBO and FAS, and introduction and passage of a City Council Bill. To initiate supplemental legislation, SDOT notifies CBO of the proposed transfer of funds, drafts the legislation and has the Law Department review the draft. SDOT also contacts the City's Director of Debt Financing to explain the proposed transfer of bond funds to a new project and provide

a new spending plan. The supplemental legislation then goes to the City Council committee responsible for finance and budget for discussion and recommendation to the Full Council for approval. Any special public outreach and comment process will add time to this process.

Seventy-six Percent of Re-purposed Bond Funds Addressed SDOT's Maintenance and Repair Backlog
From 2008 through 2013, the City repurposed $61.4 million in bond proceeds from 2007-2012 LTGO bonds. Seventy-six (76) percent, i.e., approximately $46.9 million was re-purposed to projects that addressed SDOT's $1.8 billion maintenance and repair backlog.[24] Please see Appendix E for 2007-2012 bond funds that were: 1) added by the City Council to SDOT's project appropriations, and 2) re-purposed from other City projects to SDOT projects or from SDOT projects to other SDOT projects, as of December 31, 2013.

Recommendation 1:
To facilitate shifting bond funds among different projects when there are excess bond proceeds, the City Council could consider increasing threshold amounts for transfers that require supplemental legislation.

Recommendation 2:
SDOT should work with CBO, FAS, and the Law Department to explore changes to SDOT's CIP structure to enable greater flexibility in moving bond funds among projects. For example, grouping similar projects under one project title in the CIP, as was done with the Bridge Rehabilitation list of Bridging the Gap projects, could provide SDOT greater flexibility in re-purposing bond funds among its projects.

Factor 7: Grant and other outside funds take priority in spending over bond funds.

SDOT applies for many grants and other outside funds to leverage local funds in its capital projects, but is never certain which grants and outside funding it will receive. Grant funding (and other outside funding), once awarded, often carries a condition that the funding be spent immediately. Consequently, grant funds take priority over spending of bond funds which are more flexible. For example, SDOT received a $15.4 million grant from the American Recovery and Reinvestment Act for the Spokane Viaduct Project in 2009[25], which delayed spending the same amount of 2009 bond proceeds for approximately two years. Grant funding is project-specific, whereas other local funding, including bonds, may be shifted to other priorities, subject to funding source restrictions. As a result, SDOT's practice is to spend grant funding first. This can delay the spending of bond funds.

According to CBO's March 2013 report, the availability of grants and other outside funds was the second most common factor in SDOT not spending bond proceeds at the rate originally assumed. This accounted for:

> 14% of the bond proceeds accumulated over the period 2009 through 2012. For example, SDOT was awarded $15.4 million in American Recovery and Reinvestment Act (ARRA) funds in support of the Spokane Viaduct project after it issued bonds in 2009 for the project. This allowed SDOT to apply these bond proceeds to meet project costs in future years, not in 2009 as originally planned. Similarly, SDOT received a $30 million TIGER grant in support of the Mercer East project. Like the Spokane Viaduct, receipt of the TIGER grant allowed SDOT to apply the bond proceeds to cover project costs in future years.

[24] Data source: SDOT
[25] http://inweb.ci.seattle.wa.us/financedepartment/documents/arragrantsummariesfinal9-24.pdf, page 13

Factor 8: SDOT's cost projections include funds to cover project assumptions, risks, contingencies, and inflation that help ensure that full funding is in place before issuing contracts for a project or portion of a project. Over the life of a project, these costs may or may not be incurred. According to an SDOT official, this is required by transportation industry best practices. SDOT's Capital Projects and Roadway Structures Division develops the project budgets and spending plans[26] for SDOT's six-year CIP. However, the final funding decisions on bond amounts are made by CBO and FAS.

SDOT stated that it uses industry standards and historical data from completed projects when developing project schedules and budgets. This process results in project assumptions and a risk assessment that can affect the development of the cost estimate and spending schedule. The following issues need to be considered:

- Contingency: projects in their early stages of design have many unknowns. Therefore, in accordance with transportation industry standards, a higher level of contingency is factored into its cost estimates in the early phases. For example, contingency might be needed when a project encounters unexpected soil contamination and incurs additional mitigation expense.
- Inflation rate: price escalation is also factored into cost estimates in accordance with transportation industry standards.
- Permitting: assumptions are made about how long it will take to obtain all necessary permits; this is sometimes hard to estimate because the department does not have direct control over permit issuances.
- Resolution of discussions with stakeholders: assumptions about the length of time needed for resolution of project issues with various stakeholders is often hard to estimate; SDOT has many outside stakeholders, e.g., state and federal agencies, railroads, and citizen groups.
- Grants: assumptions are made about when grants will materialize and for what amounts. Grants are included in a project's funding plan only after they are awarded.
- Construction windows: assumptions on construction schedules are sometimes dependent on allowable construction "windows" due to fish and wildlife concerns.

SDOT bases its bond requests on projected costs that include the above factors. The City could consider basing SDOT's bond needs on less than 100 percent of its request and use interfund loans if needed, as interim funding until the next bond issue. This would help to minimize borrowing until absolutely needed. Particularly in their early design stages, the use of interim financing to fund projects until costs are better defined could reduce the amount of LTGO bonds issued.

The City's Director of Finance can authorize an immediate interfund loan for up to 90 days. To extend the term longer than 90 days, a City Council ordinance is required. SDOT officials stated that they would rarely request an interfund loan of shorter than 90 days. But even if an ordinance is ultimately needed to extend the loan beyond 90 days, SDOT would have the cash immediately for project needs, and could develop the ordinance required in the months following the loan.

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[26] SDOT uses standard estimating templates to estimate project budgets and cash needs for each project phase (design, construction, and closeout) and are broken down into quarterly spending plans for the first two years. There is also a database from which project managers can pull historical data from past, similar projects to apply to their new estimates. The spending plans are input into SDOT's project cost database system, a centralized location where all the spending plans are gathered. This system has a Summit component so that project managers can track their actual spending against budget on a monthly basis.

Recommendation 3:
The City should consider basing SDOT's bond needs on less than 100% of the project's estimated one-year cash needs and encouraging the use of short-term financing for gap funding (e.g., Interfund loans) if needed, to fund the project until proceeds from the next bond issuance become available. For this approach to work, CBO, FAS, the Mayor, and the City Council would need to support SDOT's use of short-term financing and enable SDOT to obtain it quickly and efficiently. Short-term financing should be considered for projects at their initial stages, when there are many unknowns, until more definitive project cost data is available. This would allow the project's long-term financing to be arranged during a later design phase with greater accuracy.

Action Taken: After we completed our audit fieldwork, Resolution 31553 was introduced to the City Council on October 27, 2014, which includes new policies on the use of interfund loans. Policy 11 in the Resolution states:

> When considering a request for a general government interfund loan, the DMPAC and City Council shall place priority on the use of interfund loans for:
> - Bridge financing of capital projects approved by City Council for future external debt financing.
> - Project financing for up to five years of capital projects that have secure revenue sources or are collateralized with unencumbered assets with sufficient capacity or value for repayment of the principal and interest on the loan.

<u>Factor 9</u>: SDOT typically dedicates contingency amounts for each project. It has complex capital funding plans in which contingency funds may be either from internal (e.g., bond proceeds) or external (from outside sources such as grants and partnership funds) sources. If bond funding remains at the end of the project when the contingency is being held for project closeout costs, this will delay bond spending.

Contingency is set aside to cover cost uncertainties based on past experience with similar projects. In current SDOT practice, a contingency amount is typically dedicated for each project, which increases each project cost estimate. The accumulation of individual contingencies for each project can add up to a significant amount. SDOT officials stated that although the practice of having project contingencies is consistent with transportation industry best practices, it has at times pooled contingency across multiple projects at a program level, e.g., the Bridge Rehabilitation Program and the Arterial Asphalt and Paving Program.

According to CBO's 2013 paper:

> SDOT accumulated approximately $11 million in unneeded contingency funds, representing about 4% of the proceed balances amassed over this time period [2009-2012], a majority of which resulted from the successful completion of the Spokane Viaduct project.

In 2013, SDOT re-purposed these funds to other projects through quarterly supplemental legislation.

<u>Factor 10</u>: The practice of holding onto allocated funding (which may be bond proceeds) until all project costs are identified and potential contract disputes are resolved before re-purposing the funding.

SDOT officials stated that it is SDOT's practice to hold onto funds designated for a specific project until they know that they will not need the proceeds (typically at the end of a project) or if they anticipate a significant delay of a year or more in using the funds for a particular project. This practice may result in the delay of bond spending when a project experiences significant project delays or when grant funds must be spent immediately, delaying the spending of other funds such as bond funds.

<u>Factor 11</u>: Litigation on a project slowed the use of some bond proceeds.

According to CBO's 2013 paper:

> Litigation related to the Burke Gilman trail projects has meant that SDOT has not needed the cash for the project when it originally anticipated it would need the cash at the time the bonds were sold.

<u>Factor 12</u>: City Council additions to SDOT's CIP during the annual budget process added funding and bond proceeds to a number of projects.

According to CBO's 2013 paper:

> In the case of Council additions, the greensheets often add funding and bond proceeds to complete the entire project in the first year. This is often not practical as a result of the lead-time required to develop project designs meaning SDOT cannot use the bond proceeds in the timeframe originally assumed. Examples of greensheet adds where bond funds to complete the entire project were provided in advance of design include: Cheshiahud Lake Union Trail ($1 million), Chief Sealth Trail ($2 million) and Northgate Park 5th Avenue Streetscape ($830,000).

In summary, a combination of factors at national, City, and department levels contributed to SDOT's delay in bond spending and unspent bond proceeds between 2008 and 2012.

Conclusion 3:
Although the City's annual budget process defines the basic steps involved in the planning and issuance of SDOT's LTGO bonds, the City should improve communications between FAS, CBO, SDOT and the City Council, by clarifying roles and formalizing and improving internal policies and procedures for bond planning and spending of bond proceeds.

Improved Written Procedures Needed for the City's Bond Process
We learned that the procedures SDOT, CBO, and FAS use to plan and determine bond needs for the Mayor's proposed CIP are integrated into and defined by CBO's annual budget process. The City has adopted financial policies[27] for capital planning and funding, general budget policies, and debt management policies addressing SDOT's responsibility to submit a request for estimated bond fund needs as part of its budget submittal. Ultimately, according to the Seattle Municipal Code, CBO[28] has the authority to develop and propose the Mayor's budget to the City Council, and to "carry out the adopted budget" once it is adopted by the City Council. The Finance Director[29] has the authority to issue bonds authorized by ordinance.

Despite the existence of these documents, there are still gaps in the written policies and procedures related to the bonds process, concerning the delineation of roles and responsibilities of the various responsible parties for planning, managing, spending, tracking, and reporting of bond debt.

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[27] http://www.seattle.gov/financedepartment/financial_policies.htm
[28] SMC 3.14.100 City Budget Office created-Functions, powers, and authority.
[29] SMC 3.39.035 Director of Finance-Functions and powers.

The Committee of Sponsoring Organizations (COSO[30]) states that establishing policies and procedures is an essential internal control for implementing management directives to help ensure that they are effectively carried out to achieve the entities' objectives. Control activities[31] should be defined throughout the organization at all levels and functions to help ensure the objectives are achieved. Control activities include approvals, authorizations, verifications, reconciliations, reviews of operating performance, security of assets, and segregation of duties.

Formalized policies and procedures are also essential in succession planning or if there's an absence of or a change of an individual filling a role[32]. They help to ensure that the organization keeps functioning, particularly when there are complex functions carried out by various individuals.

According to the City's Director of Debt Financing, FAS "checks in" with City departments to confirm bond amounts and spending schedules before the bonds go out to market. This is a prudent procedure to ensure that the City does not sell more bonds than is necessary. We found, however, that SDOT does not document or retain some significant communication with FAS, such as the submittal of spending plans, beyond a few years. SDOT does retain communication with FAS when "last minute" changes are requested in the issuance of bond amounts.

Recommendation 4:
FAS should establish and provide training to City departments on written formal policies and procedures related to the bonds process: delineating roles and responsibilities; planning for bond needs; and managing, tracking, and communicating spending of bond proceeds. The procedure for the final check-in between FAS and SDOT before bonds are issued should be included in the formal bond process policies and procedures. The retention requirements for significant communication related to the bond process should also be delineated in the formal policies and procedures.

According to SDOT's former Deputy Director, SDOT officials first attended a DMPAC meeting in October 2013. Before then, SDOT officials were not invited to DMPAC meetings to explain the department's bond proposals.

Recommendation 5:
The Debt Management Advisory Committee (DMPAC) should consider inviting City departments that have bond funding to attend DMPAC meetings to answer questions that might arise about their use of bond funds.

Despite recent improvements to CBO, FAS, and SDOT bond spending reports to the City Council, there is still room for improvement.

SDOT provides standardized quarterly reports to CBO (i.e., the Mayor's Quarterly Financial Reports) and City Council Central Staff (i.e., Quarterly CIP Monitoring Reports); SDOT also provides reports to these entities on an as-requested basis. Please see Appendix F for a chart listing the several standardized reports SDOT provides to FAS, CBO, and City Council Central Staff.

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[30] The Committee of Sponsoring Organizations of the Treadway Commission is a joint initiative of the American Accounting Association, the American Institute of CPAs, Financial Executives International, the Association of Accountants and Financial Professions in Business, and the Internal Institute of Internal Auditors dedicated to providing thought leadership through the development of frameworks and guidance on enterprise risk management, internal control and fraud deterrence.
[31] http://www.internalcompliance.com/docs/Summary%20of%20COSO%20Internal%20Control%20Framework.pdf
[32] COSO, Internal Control-Integrated Framework, Framework and Appendices, May 2013, page 51

Although SDOT did communicate its unspent bond balances and bond spending delays in these reports, the receiving entities, particularly the City Council, would have had to study and extract the desired data from the numerous spreadsheets containing extremely detailed data.

The optimal time for communicating these data to the City Council should be determined by City Council. Council Central Staff said the best time for the City Council to receive this data is during the period when the Council is reviewing the budget submitted by the Mayor. However, Central Staff said they are often too busy to thoroughly analyze the data so they must rely on the City's Director of Debt Financing. During its budget deliberations the City Council can raise questions and concerns about SDOT's bond issuances and unspent proceeds. This is the Council's principal opportunity to make revisions to the proposed bond issuance before the bond ordinance is passed, along with the budget and the CIP, in November each year.

Recommendation 6:
If unspent bond balances continue to be a concern of the City Council, CBO and SDOT could provide the Council, during the budget process, with summarized data on unspent bond proceeds by each bond issue, and the reasons for any spending delays.

In our review of SDOT's bond monitoring reports, we found that $2 million from the 2008 bond issuance was not tracked in these reports. The proceeds were applied to the South Lake Union Streetcar project. These bond proceeds should have been included and tracked in SDOT's bond monitoring reports.

Recommendation 7:
SDOT should include and track all bond proceeds in bond monitoring reports.

Conclusion 4:
The City's Debt Management Policies[33] were last updated in 2003 and some of them do not reflect the City's current practices for the issuance and management of debt.

We identified following policies in the City's current Debt Management Policies that do not reflect the City's current practices for the issuance and management of debt:

1. The Debt Management Policies (DMP) will be reviewed and updated as needed on a five-year cycle, with the next update scheduled for 2006. (DMP Introduction)
2. All requests to incur indebtedness of more than $50,000 will be presented by memo from the requesting Department through the Director of Finance, to the DMPAC. The memo shall specify the purpose of the borrowing, any options for financing the project without borrowing, and specific sources of payment of debt service. It shall include, as specified by the Director of Finance, a detailed project budget, specifying all sources and uses and a detailed project cash flow showing all project expenses and revenues, including anticipated interest earnings. The cash flow will be shown on a quarterly basis for the first two years of the project (or until the project is completed, if less than two years are required) and on an annual basis thereafter. (DMP Policy 22)

33 http://inweb.ci.seattle.wa.us/fas/finance/documents/debtpolicies2003.pdf

3. After obtaining approval by the DMPAC, the requesting Department shall, in conjunction with the City's Bond Counsel, Office of the City Attorney, and Director of Finance, produce ordinance(s) and, if needed, resolutions for consideration by the City Council. (DMP Policy 23)
4. Before the sale of general obligation bonds, the requesting Department will submit a "Sources, Uses, and Payment" memo, to the Director of Finance identifying source and use of bond proceeds, Funds, and/or Sub-Funds and/or other accounting units for deposit of all bond proceeds, and Funds and/or Sub-Funds and/or accounting units for payment of debt service. No bonds or other forms of general obligation indebtedness shall be incurred by the City without submission of a "Sources, Uses, and Payment" memo. (DMP Policy 23)
5. The Department of Finance shall prepare an annual report on City debt and present it to the City Council at the time the mayor submits his or her Proposed Budget. This report will describe any bond issues planned for the coming year and will describe bonds issued during the current year. The report shall also provide historical and projected information on debt, including debt capacity and debt service analyses. (DMP Policy 6)

The current Debt Management Policies indicate that they were last revised in May 2003. CBO stated that items 2, 3, and 4 above are now incorporated in the City's "budget process", and the required information is part of a department's budget submittal, rather than being communicated by memo as the policies state. FAS stated that for item 5 above, debt reporting by the Director of Finance is defined in the Seattle Municipal Code[34]. Additional debt reporting is contained in the Debt Service section of City's Adopted Budget, an annual July DMPAC report, and in the City's CAFR (Comprehensive Annual Financial Report). It would require relatively simple amendments to the Debt Management Policies to take note of these changes in practice.

Recommendation 8:
The City's Debt Management Policies should be updated to reflect the City's current practices for the issuance and management of debt.

Action Taken: After we completed our audit fieldwork, Resolution 31553 was adopted by the City Council on November 24, 2014 to update and revise the City's Debt Management Policies. The policies identified above that did not reflect the City's practices at the time of our audit field work have been addressed by this resolution.

[34] SMC 3.39.035G: Report not less than quarterly to the Council's Finance & Budget Committee, or its successor committee, the performance of all major tax and fee revenue streams; the status of the City cash pool, including cash totals, performance of investments made from the pool, and the status of any and all interfund loans; and the status of City debts, debt service, debt capacity, and debt guarantees.

APPENDIX A: OVERVIEW OF CITY ENTITIES, THEIR ROLES AND RESPONSIBILITIES IN THE CITY'S LTGO BONDS PROCESS

<table>
<tr><th colspan="3">Chart 3: Overview of Entities, Their Roles and Responsibilities in the City's LTGO Bonds Process</th></tr>
<tr><td>Entity</td><td>Responsible for these Activities:</td><td>Responsible for these Decisions:</td></tr>
<tr><td>SDOT</td><td>▪ Developing project cost estimates and spending schedules for the budget and CIP.
▪ Proposing project funding plans for the CIP.</td><td>SDOT proposes a budget, including its request for bond funding for capital projects, in July each year.</td></tr>
<tr><td>CBO</td><td rowspan="4">▪ Reviewing and finalizing funding plans for the budget and CIP.
▪ Approving bond amounts in the Mayor's proposed budget and CIP.</td><td rowspan="4">The Budget Director, Director of Finance, the FAS Director of Debt Financing, and DMPAC review SDOT's proposal and arrive at the final bond amounts in the Mayor's proposed budget and CIP.</td></tr>
<tr><td>Mayor</td></tr>
<tr><td>FAS</td></tr>
<tr><td>DMPAC</td></tr>
<tr><td>City's Budget Director, Finance Director and Director of Debt Financing</td><td>▪ Checks in with departments to refine bond funding request before bond issuance.</td><td>▪ Proposes final amount for the bond issuance to the City Council, following CBO, DMPAC, and Mayor's Office approval.</td></tr>
<tr><td>City Council</td><td>▪ Reviewing/revising bond amounts in the Mayor's proposed budget and CIP.
▪ Reviewing quarterly departmental proposals for revisions to uses and amounts of bond funds in the CIP.</td><td>▪ Reviews and approves bond amounts for the City's Adopted Budget and CIP.
▪ Approves revised uses and amounts of bond proceeds via quarterly amendments to the budget (generally called Supplemental Budget Ordinances).
▪ Council passes a resolution to authorize the bond sale.</td></tr>
</table>

APPENDIX B: CITY BUDGET OFFICE ANALYSIS OF SDOT SPENDING PATTERNS ON LTGO BOND PROCEEDS (MARCH 19, 2013)

Overview

An evaluation of the Seattle Department of Transportation (SDOT) limited tax obligation (LTGO) bond proceed balances shows that SDOT has not been spending down proceeds at the rate assumed when the bonds were issued. This is not a recent development. In 2008, SDOT ended the year with $71.2 million of unused bond from multiple bond sales over several years.

Beginning in 2007 and 2008, the amount of bonds issued annually for SDOT projects increased substantially. By the end of 2011, it was clear the pace of SDOT spending did not match the amount of bond funds available. For 2012, the City took proactive steps to significantly reduce the amount of bonds issued for SDOT projects - $15.9 million as compared to an average of $68 million annually between 2008 and 2011. The City is taking additional proactive measures in 2013. The LTGO bond ordinance proposed by the Executive and currently under consideration by the Council recommends issuing no LTGO bonds for SDOT's general needs, recommending instead that SDOT use its existing bond proceed balances to cover $28.1 million in general capital needs for 2013.[35] These actions are critical as they will allow SDOT to spend down remaining bond proceeds before the City issues additional debt for SDOT projects.

The remainder of this document provides historical context to describe the bond proceeds trends, as well as proactive steps the City has already taken to date and will take in the future to more closely align the selling of bonds with SDOT's cash flow needs.

Summary of SDOT's LTGO Bond Proceed Balances 2008-2012

Bond Issue year	Bonds Issued	Unused Bond Proceeds Year End 2008	% Unspent 2008	Unused Bond Proceeds Year End 2009	% Unspent 2009	Unused Bond Proceeds Year End 2010	% Unspent 2010	Unused Bond Proceeds Year End 2011	% Unspent 2011	Unused Bond Proceeds Year End 2012	% Unspent 2012
2002-2008*	129,240,000	71,240,956	55%	18,313,173	14%	9,945,185	8%	7,945,361	6%	4,952,246	4%
2009**	64,350,877			40,428,717	63%	30,217,915	47%	12,276,028	19%	649,292	1%
2010	74,636,324					51,163,207	69%	36,349,550	49%	8,139,426	11%
2011	61,686,588							55,250,843	90%	38,966,767	63%
2012	15,884,980									10,850,020	68%
Total	345,798,769	71,240,956		58,741,890		91,326,307		111,821,782		63,557,751	18%
Notes:											
* Some bonds issued in 2002, 2005, 2008 were for 2 years.											
**Some bonds issued in 2009 were for 2 years; 41,765,877 was intended for use in 2009 and 22,585,000 was intended for use in 2010.											

Trends Contributing to the Accumulation of SDOT Bond Proceeds

The City Budget Office (CBO) worked with SDOT to conduct an extensive review of bond spending patterns between 2009 and 2012. For each project for which bonds were issued, by annual bond issuance, SDOT identified:

- Amount of bond proceeds assumed in the adopted CIP
- Amount of bond proceeds actually issued for the project
- Amount of bond proceeds actually spent by the end of each year
- Difference between actual expenditures and the amount of bonds issued

The differences between actual expenditures and the amount of bonds issued each year are what has allowed SDOT to accumulate unused bond proceeds over the period analyzed. In these instances, SDOT

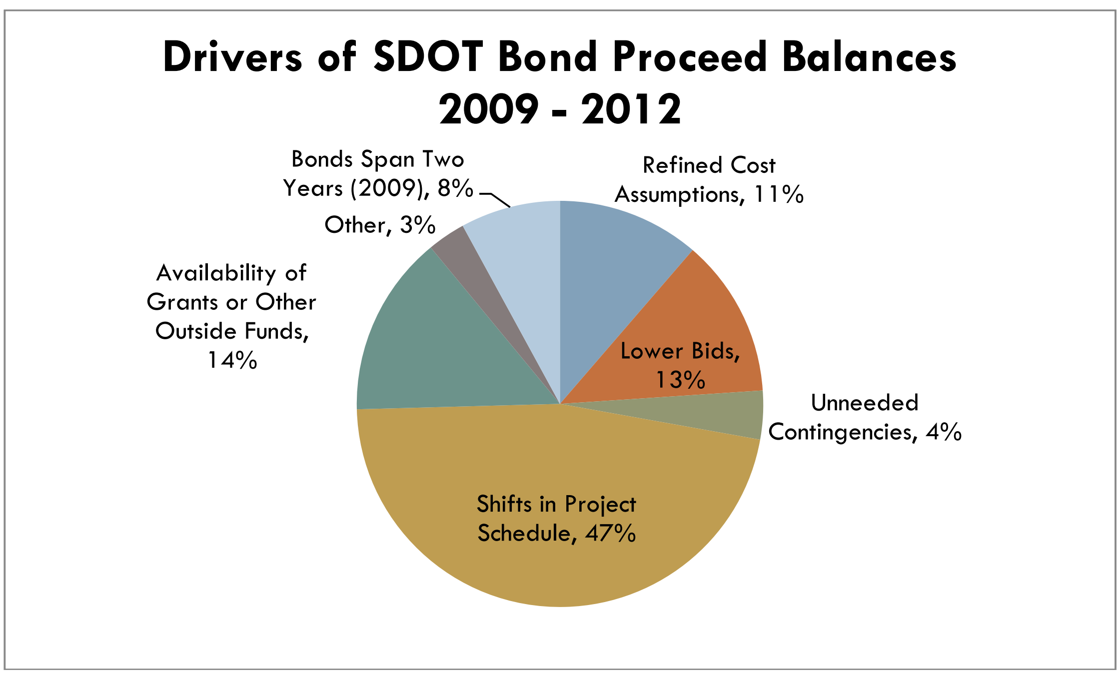
[35] The only LTGO bonds that will be issued for SDOT in 2013 are $6.2 million in seawall bonds, which are supported by the commercial parking tax.

identified and quantified the factors that contributed to the difference. Reasons for accumulating bond proceed balances include:

- Shifts in project schedules
- Availability of grants or funding from City partners
- Lower bids
- Refined cost assumptions
- Bond issuances that were intended to cover a two year period (2009)
- Contingencies not needed to the extent originally assumed
- Other miscellaneous reasons

It is important to note that this analysis amalgamates the amount of bond proceeds not needed each year over a four year period spanning over 2009 through 2012. Many of the projects financed over this period take several years from project start to project completion, with financing variables in play every step along the way. The numbers discussed in this section represent running totals of the unused proceeds in each year, some of which may eventually result in net savings at the completion of each project and some of which may represent double counting due to the carry-forward of bond balances from one year to the next. Over time, SDOT spent most of these balances by the end of 2012 as demonstrated by the fact that SDOT's actual balance of bond proceeds at the end of 2012 is $63.6 million from $346 million in total bonds issued as far back as 2002. The point of this analysis is to demonstrate that for a variety of reasons, SDOT is not spending its bond proceeds at the rate assumed when bonds were issued each year. This analysis does **not** suggest that SDOT will not need these funds over time. Rather, the analysis suggests that the City would benefit from some additional fine-tuning of the amount of bonds issued to more closely reflect SDOT's dynamic cash flow needs.

It is also important to note that the City typically sells bonds in the late spring. By definition, departments need to reserve some proceeds from the previous year's bond sale to meet cash flow needs for the initial months of the following year.



Shifts in Project Schedules: The project-by-project, bond issue-by-issue analysis completed by SDOT shows that the largest percentage of bond proceed balances accumulated over 2009 and 2012 are the result of shifts in project schedules (47%). The complexity and size of the projects managed by SDOT in this time period increased dramatically as compared to earlier time periods. Many of these projects involved other partner agencies such as the Washington State Department of Transportation (WSDOT). Often, SDOT's work is dependent on partner agencies completing their portions of the work.

Because shifts in project schedules can happen on a project over multiple years, the prevalence of this variable in driving unused bond proceed amounts can happen with a greater frequency than the other variables described in this analysis. For example, in 2010, $6.3 million in bonds issued that year for the Spokane Street Viaduct project were not spent in 2010 due to a delay in obtaining approvals from WSDOT to construct the eastern-most section of the bridge. As a result, SDOT could [not][36] advertise the project for bids, which then caused additional delays on spending the proceeds in 2011 and 2012. By the end of 2012, $603,000 of these bond proceeds had not been spent as a result of the 2010 delay in obtaining permits from WSDOT. To demonstrate how this plays out over the life of this analysis, SDOT accumulated on a running total basis $61.7 million of unused bond proceeds over the period between 2009 and 2012 as a result of schedule shifts related to WSDOT and other variables. This $61.7 million does not represent savings as most of the funds were simply spent at a later time. The net savings at the end of the Spokane Street project is approximately $14 million.

It is important to note that shifts in project schedule cannot be equated with delays in project completion. In fact, SDOT has a strong record of completing projects on schedule. The shifts described here are related to delays in when the cash is actually needed to complete the work.

Availability of Grants and Other Outside Funds: The second most common factor in SDOT not spending bond proceeds at the rate originally assumed is the availability of grants or other outside funds after the bonds were issued. This accounts for 14% of the bond proceeds accumulated over the period 2009 through 2012. For example, SDOT was awarded $15.4 million in American Recovery and Reinvestment Act (ARRA) funds in support of the Spokane Viaduct project after it issued bonds in 2009 for the project. This allowed SDOT to apply these bond proceeds to meet project costs in future years, not in 2009 as originally planned. Similarly, SDOT received a $30 million TIGER grant in support of the Mercer East project. Like the Spokane Viaduct, receipt of the TIGER grant allowed SDOT to apply the bond proceeds to cover project costs in future years.

Lower Bids: The third most common factor driving the build-up of bonds proceeds, accounting for 13% of the accumulated proceeds over the period 2009 through 2012, is SDOT receiving lower-than-anticipated bids from outside vendors. At the height of the economic downturn, SDOT benefited greatly from a number of bids coming in lower than anticipated. In fact, 26% of the proceeds not needed in 2010 were the result of bids coming in lower than anticipated. This resulted in savings in a number of projects, including the Bridge Rehabilitation and Replacement Program. For example, it cost the City $19.2 million less to replace the 45th Street Viaduct structure as a result of the contractor providing an alternate design and construction method. As a result, SDOT needed less bond proceeds than originally anticipated when the bonds were issued. As is the case when outside funding becomes available, SDOT shifts the remaining bond proceeds over time to meet other needs.

Refined Cost Assumptions: Approximately 11% of the bond proceeds accumulated between 2009 and 2012 is the result of refined cost assumptions. It is important to understand that cost assumptions for projects – particularly larger projects – are refined and subject to change over time. A cost estimate used to build the adopted budget is typically developed many months before the project actually commences. In that period of time, SDOT is continually refining and fine-tuning its cost assumptions. Most of the refined cost assumptions related to SDOT's bridge rehabilitation and seismic programs where SDOT was completing several different bridge projects in tandem (e.g., East Duwamish, 15th Ave NE, Jose Rizal, Airport over Argo, NE 45th Street).

[36] The Office of City Auditor inserted this word to clarify this sentence.

As a result of cost savings and the receipt of a $4.6 million federal grant, SDOT was able to begin design on two additional bridges, Fairview and Yesler. Spending plans and cost estimates were adjusted accordingly.

Multi-Year Bond Sales: The City had an earlier practice of issuing bonds to cover two-year's worth of cash flow needs as a strategy for taking advantage of relatively strong reinvestment rates. This practice was in place with the 2009 bond sale. Of the $64.4 million in bonds issued in 2009, $22.9 million were intended to cover cash flow needs in 2010 – mostly in the first quarter. This practice in 2009 accounts for 8% of the unused bond proceeds accumulated over the period 2009-2012.

Unneeded Contingencies: As projects near their final stages, SDOT issues bonds to cover contingencies to avoid instances of unexpected cost overruns. Over the period of this analysis, SDOT accumulated approximately $11 million in unneeded contingency funds, representing about 4% of the proceed balances amassed over this time period, a majority of which resulted from the successful completion of the Spokane Viaduct project. SDOT is currently developing options for Mayor and Council consideration for re-programming all of the unneeded proceeds from the Spokane Viaduct project to other priorities.

Other: The "other" category represents approximately 3% of the accumulated bond proceeds over this period and includes variables such as litigation or projects added by Council as it adopts the budget. For example, litigation related to the Burke Gilman trail projects has meant that SDOT has not needed the cash for the project when it originally anticipated it would need the cash at the time the bonds were sold. In the case of Council additions, the greensheets often add funding and bond proceeds to complete the entire project in the first year. This is often not practical as a result of the lead-time required to develop project designs, meaning SDOT cannot use the bond proceeds in the timeframe originally assumed. Examples of greensheet adds where bond funds to complete the entire project were provided in advance of design include: Cheshiahud Lake Union Trail ($1 million), Chief Sealth Trail ($2 million) and Northgate Park 5th Avenue Streetscape ($830,000).

Corrective Measures to Ensure the City Aligns the Sale of LTGO Bonds with SDOT's Cash Flow Needs

Aligning the size of the LTGO bond sales with actual cash flow needs is critical to the City minimizing interest costs on the borrowed funds. While spending 100% of bond proceeds in the year the bonds were issued is not practical, it is important that bond proceeds are spent in a timely manner. To address this, the City has taken the following actions:

Corrective Measures Taken To Date:

- **2011 Code and CIP Budget Policy Change** – SMC was amended to allow for partial appropriation of multi-year projects. This code change allowed CBO to implement a policy to match CIP appropriations for multi-year projects to annual spending plans. Prior to this change, departments sought, in some cases, appropriation for the entire cost of a project ahead of when spending was planned. This policy change provides additional clarity around planned spending amounts for the coming year and is an additional check when determining bond amounts.
- **Evaluation of Existing Bond Proceeds and Planned Spending** – Subsequent to adoption of the 2013-2018 CIP, an updated analysis of existing bond proceeds as of yearend 2012 and planned spending in 2013 was done to reassess financing needs prior to bond issuance.

Results:

- **Decreased the amount of bonds issued for SDOT in 2012** - $15.9 million in 2012 as compared to an average of $68 million in the years 2008-2011 and as compared to $31 million in bond proceeds assumed for SDOT in the Adopted CIP.
- **No bonds will be issued in 2013 for general SDOT needs** – SDOT will spend down bond proceed balances to meet its anticipated $28.1 million in general cash flow needs for 2013. The only limited

tax obligation bonds that will be issued for SDOT in 2013 will be $6.2 million for the seawall. This compares to $34.3 million in bond proceeds assumed for SDOT in the Adopted CIP.

Next Steps and Additional Corrective Measures:

- **Establish More Stringent Reconciliation Requirements – CBO Will Conduct Semi-Annual Reviews of SDOT's Balances as Compared to Spending Plans:**
    - Proposed Budget Phase: CBO will work with SDOT to reconcile balances in all CIP projects to date as compared to the most recent spending plans. Balances will be compiled. Through the budget process, CBO will recommend how the balances are re-allocated as the subsequent year's spending plans are established.
        - Share results with Council as part of the proposed budget transmittal.
    - Early in the Fiscal Year: The spending plans adopted for the current fiscal year will be re-evaluated early in the fiscal year by CBO and FAS to inform the size of the bond sale. CBO and FAS will also evaluate/reconcile the balances in the SDOT capital projects for the previous year to also inform the amount of capital needs for the 2014 bond sale.
        - Share results with Council as part of the bond sale ordinance.
    - Spring: Bond Sale.

- **Establish Quarterly Reporting Metrics to Monitor SDOT's Spending Against Cash Flow Plans –** CBO will work with SDOT to establish metrics that will document:
    - Planned versus actual progress
    - Identify where funding shifts have occurred
    - Align with semi-annual reconciliation process described above

- **Conduct Analysis of Bond Proceed Balances for Other City Funds**
    - CIP budgeting in the City of Seattle is very decentralized. CBO will begin doing a similar analysis of bond proceed trends on other funds, focusing on those departments who rely on General Fund or REET to cover debt service costs

- **Establish Policies Around the Use of the Cash Pool to Cover Contingency Costs –** FAS and CBO will develop policies to inform the 2014 budget around the use of the cash pool to cover capital contingency costs. This will also include an examination of policies that could govern how contingencies are sized.
    - Will coordinate with Council on the timing – likely similar to the timing of the Rainy Day Fund policy changes – in advance of the budget.

APPENDIX C: COMPARISON OF 2008-2012 PROJECTED TO ACTUAL SPENDING BY SDOT WITH BOND PROCEEDS

The City's Director of Debt Financing provided us with SDOT's projected spending of bond proceeds for the 2008-2012 bond issuances. As shown in row C for each bond issuance in the chart below, SDOT projected that 100% of the proceeds would be spent in about 2 years. Row E, which is derived from data, provided by SDOT, shows for each bond issuance the actual percent spent.

Chart 4: Summary Comparison of Projected to Actual Spending (as of 4th Quarter 2013)

A	**2008 Bond Issue**	**Beginning Balance** 65,187,202	**Q4 2008**	**Q4 2009**	**Q4 2010**	**Q4 2011**	**Q4 2012**	**Q4 2013**
B	Projected Balance		57,095,320	932,320	0	0	0	0
C	**Projected % Spend**		**12%**	**99%**	**100%**	**100%**	**100%**	**100%**
D	Actual Balance		48,936,203	20,047,449	11,945,185	9,945,361	6,952,246	212,813
E	**% Actual Spent**		**25%**	**69%**	**82%**	**85%**	**89%**	**99.7%**
A	**2009 Bond Issue**	**Beginning Balance** 64,350,877	**Q4 2008**	**Q4 2009**	**Q4 2010**	**Q4 2011**	**Q4 2012**	**Q4 2013**
B	Projected Balance			27,784,917	0	0	0	0
C	**Projected % Spend**			**57%**	**100%**	**100%**	**100%**	**100%**
D	Actual Balance			40,428,717	30,177,916	12,236,029	609,292	406,477
E	**% Actual Spent**			**37%**	**53%**	**81%**	**99.1%**	**99.4%**
A	**2010 Bond Issue**	**Beginning Balance** 74,636,324	**Q4 2008**	**Q4 2009**	**Q4 2010**	**Q4 2011**	**Q4 2012**	**Q4 2013**
B	Projected Bal				8,227,663	0	0	0
B	**Projected % Spend**				**89%**	**100%**	**100%**	**100%**
D	Actual Balance				51,133,207	36,349,551	8,139,427	4,218,322
E	**% Actual Spent**				**31%**	**51%**	**89%**	**94%**
A	**2011 Bond Issue**	**Beginning Balance** 61,686,588	**Q4 2008**	**Q4 2009**	**Q4 2010**	**Q4 2011**	**Q4 2012**	**Q4 2013**
B	Projected Balance					14,614,270	0	0
C	**Projected % Spend**					**76%**	**100%**	**100%**
D	Actual Balance					55,250,843	38,808,519	12,402,352
E	**% Actual Spent**					**10%**	**37%**	**80%**
A	**2012 Bond Issue**	**Beginning Balance** 15,935,000	**Q4 2008**	**Q4 2009**	**Q4 2010**	**Q4 2011**	**Q4 2012**	**Q4 2013**
B	Projected Balance						12,100,000	0
C	**Projected % Spend**						**24%**	**100%**
D	Actual Balance						10,800,000	7,094,304
E	**% Actual Spent**						**32%**	**55%**

Source Data: Row B (Projected Balances) for each bond issuance from FAS. Beginning balances and Row D (Actual Balances) for each bond issuance from SDOT.

APPENDIX D: PROCESS AND CONSIDERATIONS FOR RE-PURPOSING BOND FUNDS

Process for Re-purposing Bond Funds
Unused bond proceeds can be re-purposed via two mechanisms: a "budget transfer" and a "budget revision". For many years, these two actions have been addressed in section 4c of the City's annual budget legislation[37], which establishes limits on the amount of funds that can be transferred without legislation.

Capital Budget transfer: SDOT can transfer up to $999,999 in funds[38] allocated to a particular project between CIP projects within a Budget Control Level (BCL)[39]. It can also transfer up to $500,000 across BCLs without supplemental legislation. Once SDOT makes the decision to transfer the bond funds in this way, SDOT submits a "budget journal entry" to CBO for approval. When CBO approves it, FAS posts the entry.

Capital Budget revision: For transfer of funds in excess of the limits for budget transfers described above, legislation is required. This is done through amendments to each year's budget ordinance (informally called supplemental budget legislation).

Since 2004, the Section 4(c) of the ordinance adopting the budget and CIP, sets the allowable the maximum allowable transfer limit at $1 million within a BCL. This results each year in multiple projects that must await the legislative process for approval of funding transfers.

Considerations for Re-purposing Bond Funds That Require Legislation
According to SDOT, many factors need to be considered and work together when re-purposing funds from one project to another, such as:

1. A project getting re-purposed funds has to be appropriated in the budget.
2. A project must meet bond eligibility[40] requirements.
3. The funding source of the bond debt service may limit how the bond proceeds can be moved around, and in such cases, re-purposing bond proceeds can be done only within their respective funding source "buckets".[41] For example, we list in the following chart, three sources of bond debt payment: the Commercial Parking Tax (CPT), the General Fund, and

[37] For example, for the City's 2014 Adopted Budget and CIP, see Ordinance 124349, Section 4(c): Without future Council authorization by ordinance, expenditures in 2014 on any project or program identified and assigned a project identification number in the 2014-2019 Adopted CIP for Seattle City Light, Seattle Public Utilities, or the Seattle Department of Transportation, other than expenditures pursuant to unspent capital appropriations carried forward from 2013 into 2014 in accordance with RCW 35.32A.080 and allocated to the same project or program, shall not exceed by more than $1,000,000 the amount shown as the Appropriations Total in the 2014 column for that project or program in the Adopted CIP, as that amount may be amended by ordinance. The City Budget Office shall certify to the Chair of the City Council Budget Committee a list of those unspent capital appropriations not subject to the expenditure restriction imposed by this subsection by May 1, 2014, and shall also file the list with the City Clerk. The list shall include the project identification number and the dollar amount by project or program not subject to the expenditure restriction, at minimum.
[38] There is a cumulative limit of $500,000 on non-bond transfers.
[39] There are three CIP BCLs in SDOT: 19001 (Major Maintenance/Repair), 19002 (Major Projects), and 19003 (Mobility-Capital).
[40] The project is for government/public use with only a limited percentage of private-business use, if any, and bond proceeds can be used only for the capitalized portions of projects, which include design, construction, and closeout.
[41] For example, if the bond ordinance lists BTG projects and if Council wanted to re-purpose bond funding that was originally for BTG projects to the seawall (which is explicitly forbidden in the BTG levy), the bond funding could be re-purposed to the seawall by amending the bond ordinance.

King County Proposition 2. As the chart shows, there are two components of the 12.5% Commercial Parking Tax (CPT) used to pay debt service: the 2.5% portion pays the debt service for the Alaskan Way suite of projects, the Seawall Design, and Mercer West; the 10% portion funds BTG projects.

Chart 5: Examples of Three Bond Debt Funding "Buckets"			
CPT (12.5% total tax)		General Fund	King County Proposition 2
2.5 % Portion	10% Portion	Example projects: ▪ South Park Bridge ▪ Parking Pay Stations ▪ Northgate Park & Northgate Pedestrian Bridge (Parks project where SDOT received a portion of the project) ▪ Right-of-way acquisition for the Waterfront	Trails projects, i.e., Burke-Gilman, Cheshiahud, and Northgate Way intersection, which is a part of the trails package
Example projects: ▪ Alaskan Way suite of projects (e.g., Viaduct, parking project, etc. ▪ Seawall Design ▪ Mercer West	▪ BTG projects (e.g., Spokane Viaduct, Mercer Corridor East, Bridge Rehab, Bridge Seismic, Arterial Asphalt & Concrete, King Street Station, Lander Crossing, Mercer West)		

When re-purposing bond proceeds, the debt service for the new (substituted) project has to be eligible for payment from the same funding source "bucket" as the old project. For example, the BTG suite of projects includes Spokane Street, Mercer East, and paving, so re-purposing among these projects is allowed. However, some projects such as Parking Pay Stations cannot be substituted for BTG-funded projects because the BTG levy does not allow funding Parking Pay Stations and Alaskan Way Viaduct costs with BTG funds. So if there is a slowdown on a BTG project, its funding could only be moved to other BTG-eligible projects.

4. Timing: At the end of a project, SDOT's practice is to hold onto allocated funding until project costs are identified and potential contract disputes are resolved.
5. Political considerations: Transportation projects can be highly political, i.e., of high interest to residents and businesses in the affected communities, with proponents and opponents. Because of this, SDOT must keep the Mayor's Office and City Council informed of stakeholder interest in a project, and sometimes allow time for community input on shifts in project funding and schedule.
6. A bond ordinance amendment is required if the re-purposing action changes the project list in the relevant bond ordinance.

APPENDIX E: ADDED AND RE-PURPOSED 2008-2012 BOND PROCEEDS

This chart lists 2007[42]-2012 bond funds which were: 1) added and re-purposed by the City Council to SDOT, and 2) re-purposed by SDOT to other SDOT projects, as of December 31, 2013.
Column G indicates if the project receiving re-purposed funds helps to address SDOT's maintenance and repair backlog.

Chart 6: Added and Re-purposed 2008-2012 Bond Funds

A	B	C	D	E	F	G	H
Item #	**Bond Issue**	**Added/Re-purposed Amount**	**From (Project Name)**	**To (Project Name)**	**Why**	**To maintenance and repair backlog?**	**Ordinance or Budget Transfer**
1	2007	16,300,000 (Council re-purposed from Zoo and added to SDOT)	Zoo Garage	Mercer Corridor (BTG)	Originally part of 2007 bond issue to Zoo; City Council decision to re-purpose this amount to SDOT in 2008; Zoo Garage project abandoned.	No (new facility)	Ordinance 122696 May 27, 2008
2	2008	355,350 (Council added)	N/A	King Street Station (BTG)	Not part of SDOT's original 2008 bond request; the City Council added amount to SDOT's 2008 bonds.	Yes (rehabilitation or restoration)	Ordinance 122696 May 27,2008
3	2008	9,270,000 (Council added)	N/A	Spokane Street (BTG)	Same comment as above	Yes (improved facility)	Ordinance 122696 May 27, 2008
4	2008	43,439,575 (Council added)	N/A	Mercer Corridor (BTG)	Same comment as above	No (new facility)	Ordinance 122696 May 27, 2008
5	2008	2,833,530 (Council added)	N/A	South Lander Street (BTG)	Same comment as above	No (new facility)	Ordinance 122696 May 27, 2008
6	2008 (June 18, 2008)	3,800,000 (SDOT requested re-purpose)	Mercer (BTG)	Arterial Asphalt & Concrete (BTG)	Re-purposed savings from Mercer to Arterial Asphalt & Concrete	Yes (rehabilitation or restoration)	Ordinance 124353 (Q3 2013 Supplemental) November 25, 2013
7	2009 (March 11, 2009)	4,126,585 (Council re-purposed and added to SDOT)	Jail	Spokane Street (BTG)	Council decision; Expected Jail costs originally identified in Ordinance 122848 (2009 bond ordinance) was reduced and Council re-allocated to Spokane, a portion of the 2009 bonds that had been earlier allocated to the Jail, thus reducing the amount needed to be spent on Spokane Street.	Yes (improved facility)	Ordinance 123156 November 23, 2009
8	2009 (March	130,583 (SDOT initiated	Northgate Park 5th	Arterial Asphalt &	Transferred proceeds to a different project (arterial asphalt & concrete improvements) at	Yes (rehabilitation	Budget transfer; no legislation

[42] We included 2007 bonds because of the re-purposing of $16.3 million from the Zoo Garage to Mercer Corridor (BTG) in 2008.

Chart 6: Added and Re-purposed 2008-2012 Bond Funds

A	B	C	D	E	F	G	H
Item #	**Bond Issue**	**Added/Re-purposed Amount**	**From (Project Name)**	**To (Project Name)**	**Why**	**To maintenance and repair backlog?**	**Ordinance or Budget Transfer**
	11, 2009)	re-purpose)	Ave (BTG)	Concrete – NE Northgate Rehab (BTG)	the same location	or restoration)	December 2011
9	2009 (March 11, 2009)	135,202 (SDOT initiated re-purpose)	Northgate Park 5th Ave (BTG)	NE Northgate Way Intersection & Pedestrian Improvements (BTG)	Transferred proceeds to a different project (intersection and pedestrian improvements) at the same location.	Yes (improved facility)	Budget transfer; no legislation December 2011
10	2009 (March 11, 2009)	600,000 (SDOT initiated re-purpose)	Chief Sealth Trail (BTG)	Lake Union Ship Canal Trail (BTG)	Re-purposed savings from Chief Sealth Trail to another trail improvement project.	No (new facility)	Ordinance 123702 September 12, 2011
11	2009 (March 11, 2009)	100,000 (SDOT initiated re-purpose)	Chief Sealth Trail (BTG)	Burke Gilman Trail (BTG)	Re-purposed savings from Chief Sealth Trail to another trail improvement project.	No (new facility)	Budget transfer; no legislation September 2012
12	2010 (March 11, 2010)	470,000 (SDOT initiated re-purpose)	Spokane (BTG)	King Street Station (BTG)	Transferred from Spokane to King Street Station because funds for King Street Station needed sooner than originally planned. "Paid back" to Spokane later through reduction of future budget requests for Spokane.	Yes (rehabilitation or restoration)	Budget transfer; no legislation April 2010
13	2010 (March 11, 2010)	125,000 (Council initiated re-purpose)	Alaskan Way Viaduct & Seawall	Legislative Dept	Council decision to transfer this amount to pay for a construction, cost estimation, and planning consultant for Alaskan Way Viaduct & Seawall project. The project consultant to be managed by the City Council and responsible for reviewing planning and partnership agreements with regional funding partners and WSDOT.[43]	N/A	Ordinance 123363 (crossed BCLs) July 26,2010
14	2010 (March 11, 2010)	126 (SDOT will abandon)	Pay Stations	Abandon	Surplus balance that has been earmarked for abandonment.	N/A	SDOT will abandon in 2014
15	2011 (March 1, 2011)	4,050,000 (SDOT initiated re-purpose)	Spokane (BTG)	Bridge Rehab (BTG)	Re-purposed in 2013 as part of $14.978 million Spokane Street savings.	Yes (rehabilitation or restoration)	Ordinance 124222 (7/15/2013) Special transportation supplemental to

[43] Ordinance 123363, see Fiscal Note to Council Bill No. 116923, Report Item 6.15.

Chart 6: Added and Re-purposed 2008-2012 Bond Funds

A	B	C	D	E	F	G	H
Item #	**Bond Issue**	**Added/Re-purposed Amount**	**From (Project Name)**	**To (Project Name)**	**Why**	**To maintenance and repair backlog?**	**Ordinance or Budget Transfer**
							2013 adopted budget & 2013-2018 CIP
16	2011 (March 1, 2011)	6,928,043 (SDOT initiated re-purpose)	Bridge Rehab (BTG)	Bridge Seismic (BTG)	Re-purposed in 2013 from Bridge Rehab to Bridge Seismic to reduce future bond request for Bridge Seismic.	Yes (rehabilitation or restoration)	Ordinance 124222, #2.1 (abandoned $6,928,043); Ord 124195, (6/10/2013) Q1 2013 Supplemental
17	2011 (March 1, 2011)	2,795,000 (SDOT initiated re-purpose)	Bridge Rehab (BTG)	Mercer West (BTG)	Re-purposed in 2013 from Bridge Rehab to Mercer West to reduce future bond requests for Mercer West.	No (new facility)	Ordinance 124353 (Q3 2013 Supplemental)November 25, 2013
18	2011 (March 1, 2011)	1,200,000 (SDOT initiated re-purpose)	Spokane (BTG)	Cheshiahud Lake Union Trail (BTG)	Re-purposed in 2013 as part of $14.978 million Spokane Street savings.	No (new facility)	Ordinance 124222 (7/15/2013) Special transportation supplemental to 2013 adopted budget & 2013-2018 CIP
19	2011 (March 1, 2011)	409,000 (SDOT initiated re-purpose)	Spokane (BTG)	Bridge Seismic (BTG)	Re-purposed in 2013 as part of $14.978 million Spokane Street savings.	Yes (rehabilitation or restoration)	Ordinance 124222 (7/15/2013) Special transportation supplemental to 2013 adopted budget & 2013-2018 CIP
20	2011 (March 1, 2011)	1,750,000 (SDOT initiated re-purpose)	Spokane (BTG)	Linden Ave Street Improvements (BTG)	Re-purposed in 2013 as part of $14.978 million Spokane Street savings.	Yes (Improved Facility)	Ordinance 124222 (7/15/2013) Special transportation supplemental to 2013 adopted budget & 2013-2018 CIP
21	2011 (March 1, 2011)	1,900,000 (SDOT initiated re-purpose)	Spokane (BTG)	Mercer West (BTG)	Re-purposed in 2013 as part of $14.978 million Spokane Street savings.	No (new facility)	Ordinance 124222 (7/15/2013) Special transportation supplemental to 2013 adopted budget &

Chart 6: Added and Re-purposed 2008-2012 Bond Funds

A	B	C	D	E	F	G	H
Item #	**Bond Issue**	**Added/Re-purposed Amount**	**From (Project Name)**	**To (Project Name)**	**Why**	**To maintenance and repair backlog?**	**Ordinance or Budget Transfer**
							2013-2018 CIP
22	2011 (March 1, 2011)	1,191,000 (SDOT initiated re-purpose)	Spokane (BTG)	Sidewalk Development Program (BTG)	Re-purposed in 2013 as part of $14.978 million Spokane Street savings.	No (new facility – added new sidewalks)	Ordinance 124222 (7/15/2013) Special transportation supplemental to 2013 adopted budget & 2013-2018 CIP
23	2011 (March 1, 2011)	4,500,000 (SDOT initiated re-purpose)	Spokane (BTG)	Arterial Asphalt and Concrete (Northgate Paving)	Spokane Street savings	Yes (improved facility)	Ordinance 124222 (7/15/2013) Special transportation supplemental to 2013 adopted budget & 2013-2018 CIP
24	2011 (March 1, 2011)	5,900,000 (SDOT initiated re-purpose)	Spokane (BTG)	23rd Ave Corridor Improvements (BTG)	Re-purposed in 2013 as part of additional $5.9 million Spokane Street savings.	Yes (improved facility)	Ordinance 124353 (Q3 2013 Supplemental) November 25, 2013
25	2012 (May 2, 2012)	2,430,000 (Administrative re-structure of AWVS program; no change in amount; this action required supplemental legislation)	Alaskan Way Viaduct & Seawall	Elliot Bay Seawall	SDOT re-structured Alaskan Way Viad & Seawall project into 3 projects: 1) Seawall, 2) AWVS, and 3) Waterfront program. This amount was re-purposed to the Seawall project portion.	Yes (rehabilitation or restoration)	Ordinance 124309 Q2 2013 Supplemental September 30, 2013
26	2012 (May 2, 2012)	2,517,199 (SDOT initiated re-purpose)	Bridge Rehab (BTG)	Bridge Seismic (BTG)	Re-purposed from Bridge Rehab to Bridge Seismic to reduce 2013 bond request.	Yes (rehabilitation or restoration)	Ordinance 124397 Q4 2013 Supplemental December 16, 2013

Source Data: SDOT

APPENDIX F: SDOT CIP AND BOND SPENDING REPORTS

As shown in the chart below, SDOT provides several standardized reports to FAS, CBO and City Council Central Staff on the CIP in general, and bond funding and spending plans in particular.

Chart 7: SDOT CIP and Bond Spending Reports

Report	Contains	Receiving entities
Confirmation of bond issuance amount and spend down schedule prior to bond going out for sale	FAS checks-in with SDOT in spring just before bonds are to be sold.	FAS
Estimates and spending plans for new bond needs (for following year's budget)	After the previous bond issuance, FAS checks with SDOT on bond needs and projected spending plans for the next bond issuance (generally the following spring). These requests, usually two, are synchronized with SDOT's budget submittal over the summer (i.e., in June/July/August) for the following year's budget.	FAS
Quarterly Financial Reports (referred to as the Mayor's Quarterly Report)	This report consists of an excel spreadsheet of 9 tabs. Tab 7 of this report (Bond Funded Detail) shows carryover amount (unspent bond proceeds). The carryover amount is a total of all previous bond issues; there is no breakdown of unspent funds by bond issuance.	Mayor and CBO
Quarterly CIP Monitoring Reports (referred to as Council CIP Report)	This report consists of an excel spreadsheet of 6 tabs. Tab 2 (Fund Source) shows unspent bond funds as the carryover amount. The carryover amount is a total of all previous bond issues; there is no breakdown of unspent funds by bond issuance.	Council Central Staff
Quarterly LTGO Bond Monitoring Reports – first one sent to CBO in March 25, 2013 – CBO created a report template that was revised during 2013	1. Summary of unused bond proceeds by year for 2008 and prior bond sales 2. 2010 spending of 2009 and 2010 issuances 3. 2011 spending of 2009, 2010, and 2011 issuances 4. 2012 spending of 2009, 2010, 2011, and 2012 issuances 5. 2013 spending of 2009, 2010, 2011, and 2012 issuances The City Council does not receive this report.	CBO

The City Budget Director, City Finance Director, and the City's Director of Debt Financing provided this written response to the audit in which they concurred with our recommendations.

City of Seattle

City Budget Office

MEMORANDUM

DATE: December 9, 2014

TO: David Jones, City Auditor

FROM: Ben Noble, Director, City Budget Office
Glen Lee, Director of Finance
Michael Van Dyck, Director of Debt Financing

SUBJECT: **Seattle Department of Transportation Bonds Management Audit**

Thank you for the opportunity to review and comment on the Seattle Department of Transportation Bonds Management (SDOT) Audit. We understand that the scope of the audit was to evaluate the management of SDOT bond proceeds during the period from 2008 to 2012 as well as inter-departmental communications about bond spending. The City Budget Office (CBO) and the Department of Finance and Administrative Services (FAS) recognize that aligning the sizing of bond issues with projected cash flow needs is critical to prudent financial management.

In early 2013, CBO and FAS expressed concern about SDOT's cumulative unspent bond proceeds. Multiple factors at the national, local, and departmental levels contributed to SDOT's delay in bond spending, which resulted in accumulated unspent bond proceeds between 2008 and 2012.

While spending 100% of bond proceeds within one year is not always practical, it is important that bond proceeds are spent in a timely manner. Although not previously communicated effectively to elected officials, the Executive had, in fact, already begun to reform its process for making decisions about debt financing as early as 2010, when it began sizing bond issues to meet spending projections for only a 12 month period. This effort also resulted in a substantial reduction in the amount of bonds issued for SDOT in 2012, 2013, and 2014. As a continuation of this effort, CBO and FAS are now coordinating a more systematic process for the review of debt financing proposals and for better synchronization between spending plans and bond sizing.

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We are acknowledging the need to build budgets that more accurately reflect spending plans and sharing this information with the City Council in a timely manner.

Finally, CBO and FAS developed new debt policies that were adopted by the City's Debt Management Policy Advisory Committee on October 8, 2014 and by the City Council on November 24, 2014 (Resolution 31553). These new policies address all of the concerns in the audit including a detailed description of the process for making decisions about debt financing, identification of roles and responsibilities in this process, and the establishment of criteria for the use of temporary interfund loans to bridge the timing between the City's annual bond issues and to reduce the amount of external borrowing in the early stages of a project when spending projections are the most uncertain.

We welcome your review and the benefits it has had for raising awareness about the need for better coordination and efficiency. We concur with your recommendations and appreciate the cooperation of your staff with CBO, FAS, SDOT, and LAW in developing and reviewing these recommendations.

cc: Scott Kubly, Director, SDOT
Saroja Reddy, CBO

Office of City Auditor Mission Statement

Our Mission:

To help the City of Seattle achieve honest, efficient management and full accountability throughout City government. We serve the public interest by providing the City Council, Mayor and City department heads with accurate information, unbiased analysis, and objective recommendations on how best to use public resources in support of the well-being of Seattle residents.

Background:

Seattle voters established our office by a 1991 amendment to the City Charter. The office is an independent department within the legislative branch of City government. The City Auditor reports to the City Council and an audit committee, and has a four-year term to ensure her/his independence in deciding what work the office should perform and reporting the results of this work. The Office of City Auditor conducts performance audits and non-audit projects covering City of Seattle programs, departments, grantees, and contracts. The City Auditor's goal is to ensure that the City of Seattle is run as effectively and efficiently as possible in compliance with applicable laws and regulations.

How We Ensure Quality:

The office's work is performed in accordance with the Government Auditing Standards issued by the Comptroller General of the United States. These standards provide guidelines for audit planning, fieldwork, quality control systems, staff training, and reporting of results. In addition, the standards require that external auditors periodically review our office's policies, procedures, and activities to ensure that we adhere to these professional standards.