Performance Audit Report

Use of Impact Fees in Federal Way, Olympia, Maple Valley, Redmond and Vancouver

Report No. 1000014

October 14, 2008

Washington State Auditor Brian Sonntag, CGFM

www.sao.wa.gov

A letter from State Auditor Brian Sonntag

Brian Sonntag, CGFM
Washington State Auditor

The Puget Sound Region experienced an unprecedented building boom during this decade. Impact fees' purpose is to help offset the costs of services associated with new development, such as roads, schools, fire facilities and parks.

We chose this audit to examine whether cities are effectively and efficiently using of this revenue source. We selected the five cities with the state's highest impact fee revenue from fiscal years 2004 to 2006 to find out if:

- Cities are collecting and administering impact fees appropriately and in accordance with state law.
- The public is getting what it is paying for.

Performance audits are conducted under the provisions of citizens Initiative 900. This audit was conducted on our behalf by Ernst & Young in accordance with Generally Accepted Government Auditing Standards.

Cities have an opportunity to improve transparency and access to public information by posting their annual impact fee reports on their Web sites. While cities are required by state law to report the information annually, not all cities are posting the information on their Web sites. It is good policy to make that information readily available to citizens.

We hope all cities and counties that impose imact fees will take advantage of the best practices identified in this audit.

If you are interested in following up on the audit resolution or public hearings, please check our Web site at: **http://www.sao.wa.gov/PerformanceAudit/audit_reports.htm**.

What is an impact fee? A one-time fee to offset the cost of services associated with new development. Cities can collect four types of impact fees: **School**, **fire**, **park** and **transportation** impact fees. Impact fees are intended to supplement other funding sources and state law requires that they be spent on the facilities for which they are collected.

How are they administered? State law allows municipalities that are required to or choose to plan under the Growth Management Act to assess impact fees. Cities set the rate for and collect the impact fees.

Who pays impact fees? Impact fees are charged to builders as part of the building permit process. Impact fees are typically passed invisibly from the builder to the customer.

Mission Statement

The State Auditor's Office independently serves the citizens of Washington by promoting accountability, fiscal integrity and openness in state and local government. Working with these governments and with citizens, we strive to ensure the efficient and effective use of public resources.

About the audit

Objectives

The audit was designed to determine:

1. The method each city uses to calculate impact fees based on the direction in state law (RCW 82.20.050);
2. How each city demonstrates that these fees are appropriate; and
3. How effectively each city uses impact fees to pay for public facilities that:
    - Correspond to the demand for public facilities from new development.
    - Benefit new development proportionate to its share of the financing of new or expanded facilities; and are consistent with a comprehensive plan or a capital element of a comprehensive land use plan that has been adopted in accordance with state law.

If the city does not meet these objectives, what are the resulting costs to all residents and what can be done to reduce those costs?

Additionally, the audit addressed the nine elements contained in Initiative 900, outlined on page 5 of this summary.

The audit cost $726,466.

*The complete text of Initiative 900 is available at **www.sao.wa.gov/PerformanceAudit/PDFDocuments/i900.pdf**.*

Summarized audit results

Legislature

Several of the issues identified during the audit are caused by a lack of clarity in laws governing impact fees, particularly regarding the items cities may purchase with impact fee money. For instance, Olympia interpreted the law regarding road impact fees to allow it to spend the money on bike trails. Redmond interpreted the law regarding fire impact fees to allow the City to purchase fire trucks. The law states the fees can only be spent on fire "facilities;" however the law does not define a fire facility. The Legislature has an opportunity to empower cities to improve their performance and definitively comply with state law.

Issues

The audit identified three main conclusions regarding the five cities' collection and use of impact fees.

- Lack of clarity in state law may be causing some cities to calculate and spend impact fees in a manner that could be inappropriate.
- One city is charging builders higher impact fees than they should and their fees are not supported by a capital facilities plan as prescribed by law. We recommend that city discontinue charging the fees until they are supported.
- New developments in some cities are receiving questionable benefits for the impact fees paid.

Best Practices Identified for All Municipalities

The audit identifies a number of best practices that streamline or improve the collection, assessment and use of impact fees in order to minimize the costs and maximize the benefits associated with them.

*Visit **www.sao.wa.gov/PerformanceAudit/audit_reports.htm** for:*

- *Full report*
- *Cities' responses, action plans*
- *Public hearings*
- *Cities' annual status reports*

Audit Results

Audit Issues	Audit Recommendations	Financial Impacts
1. **Capital Facilities** State law defines capital facilities for fire, transportation, park and school impact fees. However, the definitions are ambiguous, resulting in cities applying varying interpretations of the term.	The Washington Legislature should amend RCW 82.02.090 to better define capital facilities and the following terms: 1. "Fire protection facilities" 2. "Public streets and roads" 3. "School facilities" 4. Address whether transportation impact fees can be spent on multimodal transportation (i.e., biking, walking, etc.).	$876,709
2. **Fire Districts** The City of Redmond Fire Department has developed a leading practice in its relationship with Fire District 34. The fire department's method of allocating costs of new capital facilities between the city and Fire District 34 should be evaluated for use by other cities and districts.	Washington cities should be aware of the City of Redmond's leading practice in its relationship with Fire District 34 and attempt to institute a similar contract if that city has a relationship with a neighboring fire district.	A more accurate allocation of costs between a city and related fire districts.
3. **Park Zoning** Olympia may not be spending park impact fees as effectively as it could, based on the results of a citizen survey and based on other cities' use of multiple park zones.	• Olympia should consider removing the "one-half to one mile" and "10- to 20-minute walk" from its definition of a "Neighborhood Park." • Olympia should consider dividing the City into two park zones to demonstrate a clear relationship between where impact fees are collected and spent. Two zones for park impact fees would appear to be reasonable, as the City is approximately six miles across.	$36,974
4. **Interest-Bearing Accounts** • Each city uses a different method to allocate interest payments to impact fee general ledger accounts. • The City of Vancouver's method of allocating interest is a leading practice among the Cities.	• Cities should consider using technology similar to Vancouver's system that allows for daily allocation of interest and minimizes manual data entry. • Cities should not allocate interest based on a rate that is not equal to actual interest earned. • The Legislature should consider modifying RCW 82.02.070 to better define "separate interest-bearing accounts."	• Using an automated system will reduce staff time currently used in manual processes. • Accurately tracking interest income reduces the risk of errors or fraud. • Clarifying an ambiguous law will help cities.
5. **School Impact Fee Interest** Olympia and Federal Way do not remit any interest they earn on school impact fees to the school districts; therefore, the interest income is not spent on the purpose for which the impact fee was imposed, as required by state law.	Cities should allocate actual interest earnings on school impact fees collected and remit those interest earnings to the appropriate school district(s) so the interest earned on impact fees can be spent in accordance with state law.	$9,469

Audit Issues	Audit Recommendations	Financial Impacts
6. **Fire Impact Fee Schedule/ Calculation** • Olympia's fire impact fee schedule/ calculation does not effectively demonstrate the connection between growth and system improvements. Olympia does not take into account the cost of public facilities necessitated by new development or the availability of other financing. • Redmond has developed a leading practice in its fire impact fee schedule/calculation, specifically the method it uses to take into account the impacts of fire and aid calls by land use type, projected growth by land use type and the fire Capital Facilities Plan.	• Cities should be aware of Redmond's leading practice for the fire impact fees schedule/calculation. • The City of Olympia should revisit its fire impact fee schedule and consider if it is suitable to continue charging the fire impact fee. Specifically, Olympia should more effectively address RCW 82.02.050 and 82.02.060 in its calculation and demonstrate the fire impact fee it charges reasonably relates to system improvements that are reasonably attributable to growth. • Additionally, the City of Olympia should consider implementing a periodic review of its fire impact fee calculation and schedule to determine if the fee is still adequate, given the city's capital facility needs and anticipated growth.	\$185,565 – \$345,313
7. **School Impact Fee Schedule/ Calculation** Some cities that collect school impact fees are not consistently reviewing impact fee calculations prepared by school districts.	Cities should revisit their review process of the school impact fee calculation/schedule and capital facilities plan, knowing they may be involved if litigation results from the school impact fee assessed.	Cities benefit by having more confidence that the school impact fee they charge is appropriate.
8. **Transportation Impact Fee Schedule/Calculation** Redmond uses several leading practices in calculating, charging and maintaining its transportation impact fee.	• Cities should consider a construction cost adjustment to align transportation impact fees with the cost of projects they fund. • Cities that calculate impact fees based on a short-term project list should consider expanding that list to include projects farther in the future that will be needed to accommodate growth. • Cities should adopt a transportation impact fee schedule that allows developers to easily determine the impact fee to be paid upon building permit issuance. The transportation fee schedule should be based on typical land uses and trips per land use.	• Impact fees will more closely match the costs they support. • Cities may charge a fee that better represents the cost of growth. • Developers will be able to calculate and understand their transportation impact fee without outside assistance.
9. **Permit System** • Redmond inputs collection, interest earnings, and expenditure of each impact fee in a database and in the City's cash receipt system. The City is duplicating work by entering the same information twice. • Vancouver and Olympia integrated their permitting systems with their accounting systems. This is a leading practice that results in more effective internal controls and limits manual data entry.	• Redmond should eliminate database tracking of individual impact fee collection, expenditures, and interest allocation to save staff time. • All cities should maintain a permit system that automatically interfaces with its accounting system. Leading practices are in place in Vancouver and Olympia.	\$76,280
Total financial impacts: \$1.18 million to \$1.34 million		

Best Practices

Initiative 900 requires the State Auditor's Office to identify best practices during each performance audit. The following best practices were in place at the cities during the audit:

Redmond

- The City of Redmond Fire Department's method of allocating costs of new capital facilities between the City and Fire District 34 should be evaluated for implementation in other cities and districts.
- The City of Redmond's fire impact fee calculation and schedule met all aspects of the related state laws and demonstrates a leading practice by taking the following items into consideration:
  - System improvements that are reasonably related to growth
  - The proportionate share of the costs of system improvements related to new development
- Redmond employs several leading practices with respect to calculating, charging, and maintaining its transportation impact fee.
  These leading practices include:
  - Inflation indexing
  - Costs based on a long-range plan
  - Adopted fee schedules by land use

Vancouver

- The City of Vancouver uses the Emphasys SymPro system to assist in managing the city treasury function, including interest allocation. The system tracks investment earnings and interfaces with the city's general ledger to retrieve the daily balances for all accounts to which to allocate interest. Investment earnings are then allocated across the general ledger accounts based on their average daily balances.
- The City of Vancouver's school impact fee review process is a leading practice, as the City demonstrates the most in-depth and comprehensive review of the school impact fee calculation and schedule.

Vancouver and Olympia

- The cities of Vancouver and Olympia integrated their permitting systems with their accounting systems. This was identified as a leading practice among the Cities due to the tighter internal controls and minimal manual entry.

About Initiative 900

Washington voters approved **Initiative 900** in November 2005, giving the State Auditor's Office the authority to conduct independent performance audits of state and local government entities on behalf of citizens to promote accountability and cost-effective uses of public resources.

I-900 directs the Office to address the following elements in each performance audit:

1. Identification of cost savings.
2. Identification of services that can be reduced or eliminated.
3. Identification of programs or services that can be transferred to the private sector.
4. Analysis of gaps or overlaps in programs or services and recommendations to correct them.
5. Feasibility of pooling auditee's information technology systems.
6. Analysis of the roles and functions of the auditee and recommendations to change or eliminate roles or functions.
7. Recommendations for statutory or regulatory changes that may be necessary for the auditee to properly carry out its functions.
8. Analysis of the auditee's performance data, performance measures and self-assessment systems.
9. Identification of best practices.

Initiative 900 provides no penalties for auditees that do not follow recommendations in performance audit reports.

The complete text of the Initiative is available at: **www.sao.wa.gov/PerformanceAudit/PDFDocuments/i900.pdf.**

Recommendations to the Legislature

We made the following recommendations to the Washington Legislature:

- Amend RCW 82.02.090 to better define capital facilities and alleviate ambiguity.
- Consider modifying RCW 82.02.070 to better define "separate interest-bearing accounts."

What's next?

Initiative 900 requires the legislative bodies for the governments in this report to hold at least one public hearing to consider the audit results and receive comments from the public within 30 days of this report's issue.

The corresponding legislative body must consider this report in connection with its spending practices. A report must be submitted by the legislative body by July 1 each year detailing the status of the legislative implementation of the State Auditor's recommendations. Justification must be provided for recommendations not implemented. Details of other corrective action must be provided as well.

The state Legislature's Joint Legislative Audit and Review Committee (JLARC) will summarize any statewide issues that require action from the Legislature and will notify the appropriate fiscal and policy committees of public hearing agendas.

Follow-up performance audits of any state or local government entity or program may be conducted when determined necessary by the State Auditor.

Initiative 900 provides no penalties for state agencies or local governments that do not follow recommendations made in performance audit reports.

JLARC posts its I-900 public hearings and agendas at: ***http://www.leg.wa.gov/JLARC/i-900.htm***

To receive electronic notification of audit reports, sign up at:
https://www.sao.wa.gov/applications/subscriptionservices/

For more information

Washington State Auditor		
Brian Sonntag, CGFM	sonntagb@sao.wa.gov	(360) 902-0360
Director of Performance Audit		
Linda Long, CPA, CGFM, CGAP	longl@sao.wa.gov	(360) 902-0367
Communications Director		
Mindy Chambers	chamberm@sao.wa.gov	(360) 902-0091
To request a public record from the State Auditor's Office:		
Mary Leider, Public Records Officer	leiderm@sao.wa.gov	(360) 725-5617
For general information from the State Auditor's Office:		
Main phone number		(360) 902-0370
Web site		http://www.sao.wa.gov
Toll-free hotline for reporting government waste and abuse		(866) 902-3900
To find your legislator		http://apps.leg.wa.gov/districtfinder
To contact the City of Federal Way:		
Mayor Jack Dovey	jack.dovey@cityoffederalway.com	(253) 835-2401
To contact the City of Olympia:		
Mayor Doug Mah	dmah@ci.olympia.wa.us	(360) 753-8447
To contact the City of Maple Valley:		
Mayor Laure Iddings	council@ci.maple-valley.wa.us	(425) 413-8800
To contact the City of Redmond:		
Mayor John Marchione	mayor@redmond.gov	(425) 556-2101
To contact the City of Vancouver:		
Mayor Royce Pollard	mayor@ci.vancouver.wa.us	(360) 696-8211

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State of Washington
Performance Audit of Impact Fees

Ernst & Young
Quality In Everything We Do

Ernst & Young
Suite 3500
999 Third Avenue
Seattle, Washington 98104

Tel: +1 206 621 1800
www.ey.com

September 24, 2008

Washington State Auditor's Office
Brian Sonntag
State Auditor
3200 Capitol Boulevard
Olympia, Washington 98504-0031

Dear Mr. Sonntag:

We have completed our engagement to conduct an independent performance audit of impact fees in five cities within the state of Washington (Vancouver, Federal Way, Redmond, Olympia, and Maple Valley) under Generally Accepted Government Auditing Standards (GAGAS). Our engagement was performed in accordance with our engagement letter dated November 18, 2007, and our procedures were limited to those described in that letter.

Results of our work/Period covered by our procedures/ Recommendations

During the period November 18, 2007 to August 11, 2008, Ernst & Young conducted a performance audit of the five aforementioned cities' impact fees. Our *State of Washington Performance Audit of Impact Fees* report resulting from our engagement is provided in the attached report.

Background

In 2005, the voters of Washington State passed Initiative 900 (I-900) authorizing the State Auditor's Office to begin conducting performance audits of various Washington State and local government entities. The purpose of these performance audits is to promote accountability and cost-effective uses of public resources through identification of opportunities for potential cost savings. These savings can be achieved in a number of ways, such as reduction or elimination of services, implementation of best practices, change or elimination of roles and functions, and pooling of information technology. In addition to these opportunities, I-900 seeks recommendations for statutory or regulatory changes that may be necessary for the entity to carry out its functions properly.

I-900 requires performance audits conducted on behalf of the State Auditor's Office to meet GAGAS. The performance audit of the cities' impact fee processes was completed in accordance with GAGAS.

Scope of our work

The specific objectives of the performance audit were to determine:

- The method each city uses to calculate impact fees based on the direction in state law (RCW 82.02.060);
- How each city demonstrates that these fees are appropriate; and
- How effectively each city uses impact fees to pay for public facilities that:
  - Correspond to the demand for public facilities from new development;
  - Benefit new development proportionate to its share of the financing of new or expanded facilities; and
  - Are consistent with a comprehensive plan or a capital element of a comprehensive land use plan that has been adopted in accordance with state law; and if the city does not meet these objectives, what are the resulting costs to all residents and what can be done to reduce those costs?

As outlined in our engagement letter, our State *of Washington Performance Audit of Impact Fees* report to you is based on inquiries of, and discussions with, management.

Our work has been limited in scope and time and we stress that more detailed procedures may reveal issues that this engagement has not.

Restrictions on the use of our report

Ernst & Young assumes no responsibility to any user of the report other than the Washington State Auditor's Office. Any other persons who choose to rely on our report do so entirely at their own risk.

We appreciate the cooperation and assistance provided to us during the course of our work. If you have any questions, please call Michael Kucha at +1 206 654 7741 or Jason Heinz at +1 206 654 7532.

Very truly yours

Ernst & Young LLP

Attachment

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INTRODUCTION

BACKGROUND

In 2005, the voters of Washington State passed Initiative 900 (I-900) authorizing the State Auditor's Office to begin conducting performance audits of various Washington State and local government entities. The purpose of these performance audits is to promote accountability and cost-effective uses of public resources through identification of opportunities for potential cost savings. These savings can be achieved in a number of ways, such as reduction or elimination of services, implementation of best practices, change or elimination of roles and functions, and pooling of information technology. In addition to these opportunities, I-900 seeks recommendations for statutory or regulatory changes that may be necessary for the entity to carry out its functions properly.

I-900 requires performance audits conducted on behalf of the State Auditor's Office to meet generally accepted government auditing standards (GAGAS). The performance audit of the cities' impact fee processes was completed in accordance with GAGAS.

OBJECTIVE

The specific objectives of the performance audit were to determine:

- The method each city uses to calculate impact fees based on the direction in state law (RCW 82.02.060);
- How each city demonstrates that these fees are appropriate; and
- How effectively each city uses impact fees to pay for public facilities that:
    - correspond to the demand for public facilities from new development;
    - benefit new development proportionate to its share of the financing of new or expanded facilities; and
    - are consistent with a comprehensive plan or a capital element of a comprehensive land use plan that has been adopted in accordance with state law; and if the city does not meet these objectives, what are the resulting costs to all residents and what can be done to reduce those costs?

The performance audit was also planned and performed to satisfy the following objectives of I-900:

- Identification of cost savings
- Identification of services that can be reduced or eliminated
- Identification of programs or services that can be transferred to the private sector
- Analysis of gaps or overlaps in programs or services and recommendations to correct gaps or overlaps
- Feasibility of pooling information technology systems within the city
- Analysis of the roles and functions of the city and recommendations to change or eliminate city roles or functions
- Recommendations for statutory or regulatory changes that may be necessary for the city to properly carry out its functions
- Analysis of city performance data, performance measures, and self-assessment systems
- Identification of best practices

METHODOLOGY

To achieve the performance audit objectives, Ernst & Young developed a multi-phased statement of work. The project was conducted in four phases:

- **Phase 1** – Conduct a performance and risk assessment to identify improvement opportunities in the form of leading practices and/or issues. Identify areas that have the greatest opportunity to reduce costs and improve efficiency.

- **Phase 2** – Develop a work plan for the highest risk areas identified in Phase 1 to determine findings and recommendations.

- **Phase 3** – Execute the work plan.

- **Phase 4** – Issue the final performance audit report to the State Auditor's Office and assist the State Auditor's Office in presentations to state legislators, legislative committees or city councils.

Ernst & Young identified several leading practices and/or issues during Phase 1 as potential opportunities for improvement in efficiency, effectiveness, and economy. These issues were discussed and prioritized with the State Auditor's Office in order to select the leading practices and/or issues to examine further in subsequent phases of the performance audit. The conclusion of Phase 1 resulted in the State Auditor's Office selecting nine leading practices and/or issues for detailed review. These issues were selected because they were given a high-impact rating for benefits to the State of Washington and its citizens for potential improvement if performance audit recommendations are implemented. The selection of these issues narrowed the focus of Ernst & Young's scope. The new scope focused on the following nine areas:

- *Impact fee spending on capital facilities may not be consistent with RCW 82.02.050. For example, the City of Redmond spent impact fees to purchase a new fire truck, which may not be considered a new capital facility, as per Ernst & Young's interpretation of RCW 82.02.050.* ***(Area 1 – Capital Facilities)***

- *Possible spending of city impact fees on fire protection facilities located within fire district boundaries may not comply with RCW 82.02.090.* ***(Area 2 – Fire Districts)***

- *The cities of Olympia and Redmond use one zone to assess, collect and spend park impact fees. Therefore, impact fees could potentially be collected on one side of a city where the development is, but could be spent on the other side of a city; therefore, creating the question, "Are park impact fees under multiple zones being more effectively expended in areas that are most reasonably related to new growth?"* ***(Area 3 – Park Zoning)***

- *According to RCW 82.02.070, impact fees should be " . . . retained in separate interest-bearing accounts by the type of public facility for which the impact fees were collected." The Cities do not maintain impact fees in separate interest-bearing accounts. The impact fees are only maintained in separate general ledger (GL) accounts.* ***(Area 4 – Interest-Bearing Accounts)***

- *The Cities collect school impact fees on behalf of various school districts. The Cities remit the impact fees collected at the end of the month to the school districts; however interest earned on those impact fees is not remitted to the school districts. Therefore* *interest earned on the impact fees may not expended for the purpose for which the impact fee was imposed, as required by RCW 82.02.070.* ***(Area 5 – School Impact Fee Interest)***

- *Olympia uses a flat rate per square foot to assess fire impact fees, which may not indicate the development's impact on the fire system as precisely as a model considering types of property use. The model used in Redmond considers aid calls by type of property as a cost driver for the impact fees assessed.* ***(Area 6 – Fire Impact Fee Schedule/Calculation)***

- *There is inconsistency across the Cities and within the Cities regarding the school impact fees assessed on single-family residences versus multi-family residences.* ***(Area 7 – School Impact Fee Schedule/Calculation)***

- *Two Cities use land use categories to determine the transportation impact fee, and two Cities use an assessment of trips generated for each development to determine the impact fee. It is not yet clear if there is a leading practice for all Cities.* ***(Area 8 – Transportation Impact Fee Schedule/Calculation)***

- *The City of Vancouver's permit system automatically calculates impact fees and is fully integrated with its general ledger system, which is seen as a leading practice.* ***(Area 9 – Permit System)***

In Phase 2, Ernst & Young developed an audit plan for the above nine areas. The audit plan was then executed during Phase 3.

SCOPE

Ernst & Young has completed a performance audit in accordance with GAGAS of the five city's impact fee processes. GAGAS standards require that Ernst & Young plan and perform the performance audit to:

- Obtain an understanding of the area to be audited
- Consider legal and regulatory requirements
- Identify and review management controls applicable to the area

- Identify criteria needed to evaluate matter subject to audit
- Identify and examine relevant sources of data to satisfy the audit objectives
- Determine the need for technical specialist assistance

Ernst & Young tested data and records mainly related to fiscal years 2004–2006, although Ernst & Young also obtained data related to historical bienniums and data related to the most recent fiscal years for certain tests and analysis. Ernst & Young began the performance audit in November 2007 and completed fieldwork in March 2008.

SUMMARY OF PERFORMANCE AUDIT RESULTS

The performance audit focused on the nine audit areas mentioned above. The findings and recommendations related to these areas are summarized as follows:

1 – Capital Facilities

Finding	Recommendations
RCW 82.02.090 defines the term capital facilities for fire, transportation, park, and school impact fees. However, the definitions provided are ambiguous, resulting in Cities applying varying interpretations of the definition of a "capital facility."	Ernst & Young recommends that Washington State amend RCW 82.02.090 to better define capital facilities and alleviate the ambiguity.

2 – Fire Districts

Finding	Recommendations
The City of Redmond Fire Department has developed a leading practice in its relationship with King County Fire District No. 34. Specifically, the City of Redmond Fire Department's method to allocate costs of new capital facilities between the city and Fire District No. 34 should be evaluated for implementation in other cities and districts.	Other cities within the State of Washington should be aware of this leading practice and attempt to implement a similar contract if the city has a relationship with a neighboring fire district.

3 – Park Impact Fee Zones

Finding	Recommendations
The use of multiple zones is seen as an effective way to reasonably relate the collection and expenditures of park impact fees to areas experiencing growth. Based on the use of one zone, the City of Olympia is potentially spending neighborhood park impact fees that are inconsistent with its definition of a neighborhood park and results of a citizen survey. Therefore, the City of Olympia may not be spending park impact fees as effectively as it could using multiple zones.	Consider removing the "one-half to one mile" and "10–20 minute walk" from its definition of a "Neighborhood Park." And Consider dividing the City into two park zones to demonstrate a clear relationship between where impact fees are collected and spent. At least two zones for park impact fees would appear to be reasonable, given the City's six (6) mile expanse.

4 – Interest-Bearing Accounts

Finding	Recommendations
Interest allocation methods used by each City to allocate interest to impact fee general ledger (GL) accounts vary among the Cities. The City of Vancouver's interest allocation method is a leading practice among the Cities.	The Cities should consider procuring a treasury management system similar to that of the City of Vancouver, which allows for a daily allocation of interest and minimal manual involvement. Cities should allocate interest based on actual interest earned, rather than allocating interest using a rate that is near but not equal to the actual interest earned.
	Washington State should consider modifying RCW 82.02.070 to better define "separate interest-bearing accounts."

5 – School Impact Fee Interest

Finding	Recommendations
The cities of Olympia and Federal Way do not remit any interest earned on school impact fees they receive to the school districts; therefore, the interest earned while the impact fees were invested does not appear to be expended for the purpose for which the impact fee was imposed, as required by RCW 82.02.070.	The Cities should allocate both past and future actual interest earnings to school impact fees collected and remit those interest earnings to the appropriate school district(s).

6 – Fire Impact Fee Schedule/Calculation

Finding	Recommendations
The City of Redmond has developed a leading practice in its fire impact fee schedule/calculation, specifically the method it utilizes takes into account the impacts of fire and aid calls by land use type, projected growth by land use type and the fire Capital Facilities Plan (CFP). The City of Olympia's fire impact fee schedule/calculation does not appear to effectively demonstrate the fee's connection to system improvements related to growth, the cost of public facilities necessitated by new development or the availability of other financing.	Other cities within the State of Washington should be aware of the City of Redmond's leading practice for the fire impact fees schedule/calculation. The City of Olympia should revisit its fire impact fee schedule and consider if it is suitable to continue charging the fire impact fee. Specifically, Olympia should more effectively address RCW 82.02.050 and 82.02.060 in its calculation and provide support that the fire impact fee charged reasonably relates to system improvements that are reasonably attributable to growth. Additionally, the City of Olympia should consider implementing a periodic review of its fire impact fee calculation and schedule to determine if the fee is still adequate, given its capital facilities plan (i.e., the city's capital facility needs and anticipated growth).

7 – School Impact Fee Schedule/Calculation

Finding	Recommendations
Among the Cities that collect school impact fees, there are inconsistencies in determining the level of review of the school impact fee calculation prepared by the school districts.	The Cities should revisit their review process of the school impact fee calculation/schedule and capital facilities plan, knowing that they may be involved if litigation results from the school impact fee assessed.

8 – Transportation Impact Fee Schedule/Calculation

Finding	Recommendations
Redmond employs several leading practices with respect to calculating, charging, and maintaining its transportation impact fee.	Cities should consider implementing a construction cost adjustment to keep transportation impact fees in line with the cost of projects they fund.
	Cities calculating impact fees based on a short-term project list should consider expanding that list to include projects farther in the future to better compensate for long-term growth.
	Cities should adopt a transportation impact fee schedule in their ordinances that allows a developer to easily determine the impact fee to be paid upon building permit issuance. The transportation fee schedule should be based on typical land uses and trips per land use.

9 – Permit System

Finding	Recommendations
Redmond records collection, interest earnings, and expenditure of each impact fee received in an Access database. The same general information is available in the city's cash receipt system, creating a duplication of efforts by entering the impact fee information twice.	Redmond should eliminate the Access database tracking of individual impact fee collection, expenditures, and interest allocation to save staff time. This entry is a duplication of efforts, as all data entered into the database is available within the city's cash receipt system.
The cities of Vancouver and Olympia have integrated their permitting systems with their accounting systems. This was identified as a leading practice among the Cities, resulting in more effective internal controls and limiting manual manipulation.	All Cities (Vancouver, Redmond, Federal Way, Maple Valley, and Olympia) should maintain a permit system that automatically interfaces with the city accounting system. Leading practices would be the cities of Vancouver and Olympia's systems.

POTENTIAL COST SAVINGS SUMMARY

Recommendation	Potential Cost Savings and Other Impacts
Finding 1 (Audit Area 1)	$876,709 in questionable uses
Finding 2 (Audit Area 2)	• A more accurate allocation of costs between a city and related fire districts.
Finding 3 (Audit Area 3)	$36,974 in neighborhood park impact fees potentially spent greater than three miles from the development site
Finding 4 (Audit Area 4)	• Automation of interest allocation may reduce required accounting staff time. • Accurate interest allocation prevents acceptance of unsupported excesses or deficiencies in interest earnings accounts that could make these accounts prone to errors or fraud.
Finding 5 (Audit Area 5)	$9,469 in interest retained/not remitted to school districts
Finding 6 (Audit Area 6)	• $185,565 – 345,313 in potential overcharges of impact fees • May be possible that the City of Olympia has undercharged the fire impact fee, as the fire impact fee calculation is not tied to its capital facilities plan
Finding 7 (Audit Area 7)	• The Cities will have more confidence that the school impact fee they charge is appropriate.
Finding 8 (Audit Area 8)	• Fees will more closely match the costs they support. • Cities may find they are more competitive for grant funding and will charge a more accurate impact fee that better represents the cost of growth. • Developers will be able to calculate and understand their transportation impact fee without outside assistance.
Finding 9 (Audit Area 9)	$76,280 in cost savings from streamlining impact fee administration
Total Potential Cost Savings and Other Impacts	**$1.18 million–$1.34 million**

Ernst & Young recognizes that implementation of the recommendations will require resources. Although this performance audit was not structured to include detailed implementation plans and related expenses, Ernst & Young feels that the Cities have the experience and expertise to develop the specific steps necessary to implement the recommendations.

IMPACT FEE OVERVIEW

BRIEF HISTORY OF IMPACT FEES

Development impact fees are one-time charges applied to offset the additional public-service costs of new development. They are generally applied at the time a building permit is issued and are dedicated to provisions of additional services made necessary by the development of new facilities (i.e., growth) in the area. Across the United States, jurisdictions have written laws and ordinances permitting impact fees to be spent on water and sewer systems, roads, schools, libraries, fire fighting, and parks and recreation facilities. The funds collected cannot be used for operation, maintenance, repair, alteration, or replacement of existing capital facilities.

In the State of Washington, impact fees are only used to fund facilities, such as roads, schools, fire facilities, and parks that are associated with new development. In Washington, impact fees are authorized for those jurisdictions that are required or choose to plan under the Growth Management Act (GMA), RCW 36.70A.070. GMA impact fees are only authorized for public streets and roads; publicly owned parks, open space, and recreation facilities; school facilities; and fire protection facilities in jurisdictions that are not part of a fire district. Setting fee schedules for impact fees is a complex process typically involving rate studies. Fees are meant to be used in conjunction with other sources of funding.

TYPES OF IMPACT FEES ASSESSED IN WASHINGTON STATE

Impact fees are collected and spent in Washington on public facilities defined in
RCW 82.02.090:

"Public facilities" means the following capital facilities owned or operated by government entities:

(a) Public streets and roads;

(b) Publicly owned parks, open space, and recreation facilities;

(c) School facilities; and

(d) Fire protection facilities in jurisdictions that are not part of a fire district.

<u>Public Streets and Roads</u>

Impact fees for transportation are the most common impact fee managed by the Cities within the scope of the performance audit, being implemented by Redmond, Maple Valley, Vancouver, and Olympia. They are assessed on both residential and commercial development in these Cities, and they pay for projects that increase the capacity of the transportation system to accommodate additional growth. Some Cities only spend transportation impact fees on projects that improve the capacity of the road system, but one city also spends transportation impact fees on projects supporting other modes of transportation, such as sidewalks and bicycle lanes. The fundamental measure used to distribute transportation impact fees is generally the number of new trips expected to be generated from the development, based on an industry reference manual.

Publicly Owned Parks, Open Space, and Recreation Facilities

"Park Impact Fees" for short, are assessed on residential development in Olympia, Redmond, and Vancouver. In addition, Redmond has noted that in its city, the parks see significant use during typical lunch hours and has decided to assess park impact fees on residential, office, retail trade, and manufacturing land uses.

School Facilities

Impact fees for school facilities are assessed on residential development in all the Cities within the scope of the performance audit. Vancouver collects school impact fees for three separate school districts, while the rest of the Cities collect impact fees for one school district. Redmond did not collect school impact fees during our performance audit period, but subsequently began collecting school impact fees in 2007. As school districts are not managed by the city government adopting the fee, there are unique inter-jurisdictional features of school impact fees. The impact fee calculations and support are prepared by the school districts and approved by the Cities. Cities assess and collect the fees in their building permitting process and remit those fees to the school districts.

Fire Protection Facilities in Jurisdictions That Are Not Part of a Fire District

Fire impact fees are collected from residential and commercial development and are spent by city fire departments on a variety of facilities to serve development. Fire impact fees are assessed in Redmond and Olympia.

INFORMATION ABOUT THE CITIES THAT WERE AUDITED

City of Redmond

Redmond was officially incorporated on December 31, 1912. The total area of the city is approximately 16 square miles, with an estimated population of 48,739 in 2006. In 2004, 2005, and 2006, Redmond collected a total of $4,556,103 in traffic, fire, and park impact fees. In November 2006, the city implemented school impact fees. However, no school impact fees were collected in 2006.

City of Olympia

The City of Olympia, Washington State's Capitol, was officially incorporated in January of 1859. The city has a population greater than 43,000 (up 5% in the past six years) and includes an area of 18.5 square miles at the southern tip of the Puget Sound. The City of Olympia was one of the first jurisdictions to collect impact fees after the Washington State Growth Management Act became effective in 1993. Olympia assesses traffic, park, fire, and school impact fees. In 2004, 2005, and 2006, Olympia collected $7,552,925 in impact fees.

City of Vancouver

Incorporated in 1857, the City of Vancouver covers 48.5 square miles and is home to over 160,000 people. The city assesses transportation, park, and school impact fees. In 2004, 2005, and 2006, Vancouver collected a total of $24,300,539 in impact fees.

City of Maple Valley

Maple Valley was officially incorporated on August 31, 1997. The city's size is roughly six square miles, with an estimated population in 2006 of 19,140. In 2004, 2005, and 2006, Maple Valley collected a total of $6,285,349 in traffic and school impact fees.

City of Federal Way

Federal Way was incorporated on February 28, 1990. The city has a size of 21 square miles and an estimated population of 84,166 as of 2006. In 2004, 2005, and 2006, Federal Way collected $1,738,686 in school impact fees.

SUMMARY OF IMPACT FEES COLLECTED ACROSS THE CITIES

EXHIBIT 1: TRANSPORTATION IMPACT FEES COLLECTED 2004–2006

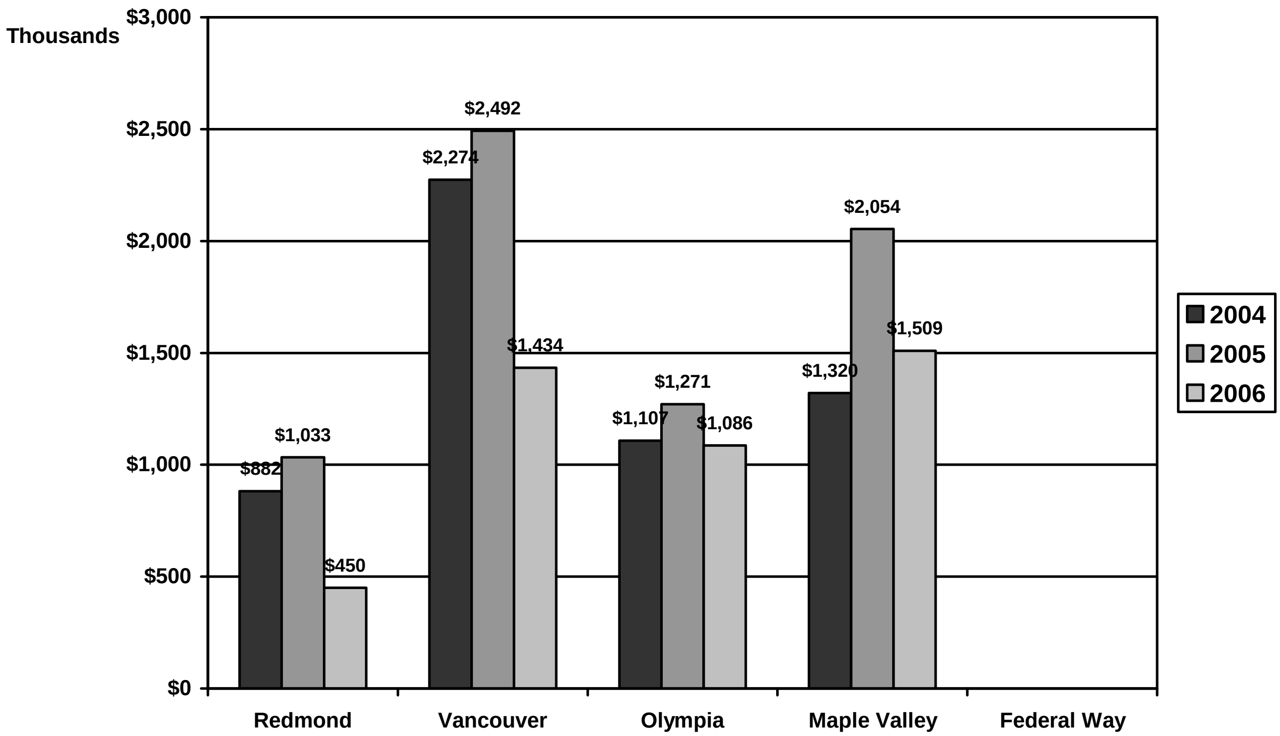


EXHIBIT 2: PARK IMPACT FEES COLLECTED 2004–2006

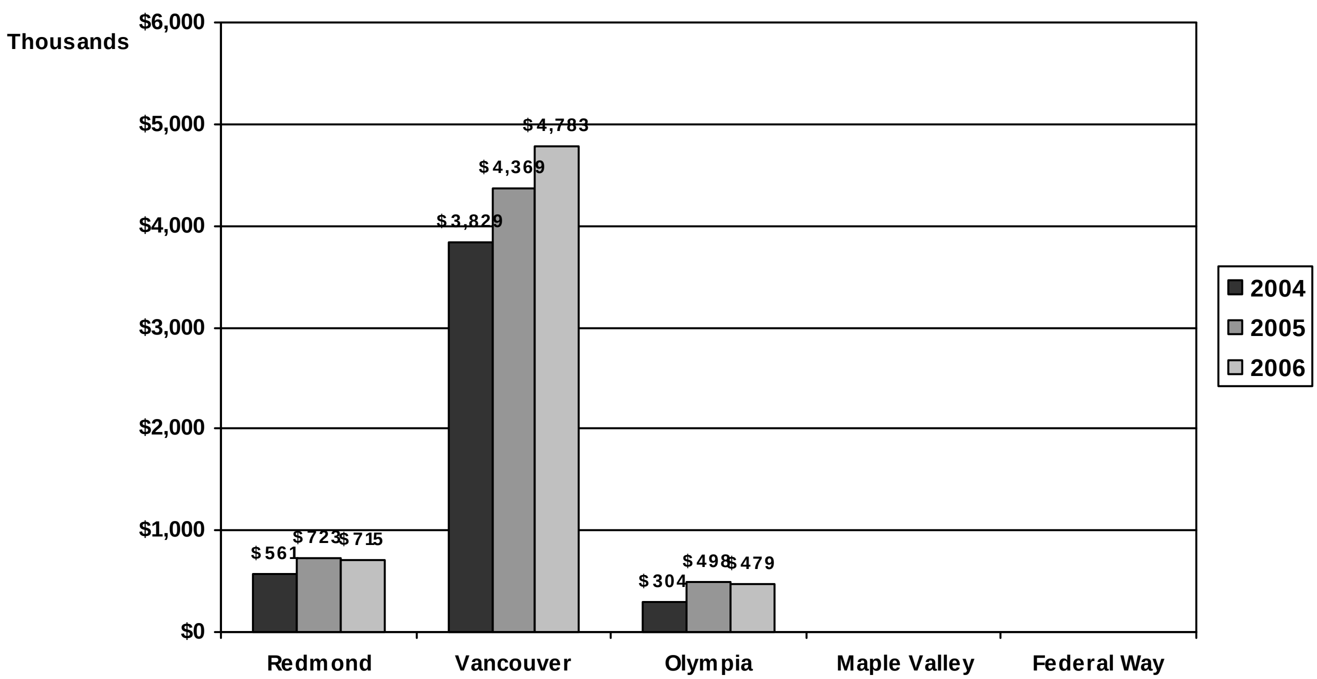


EXHIBIT 3: FIRE IMPACT FEES COLLECTED 2004–2006

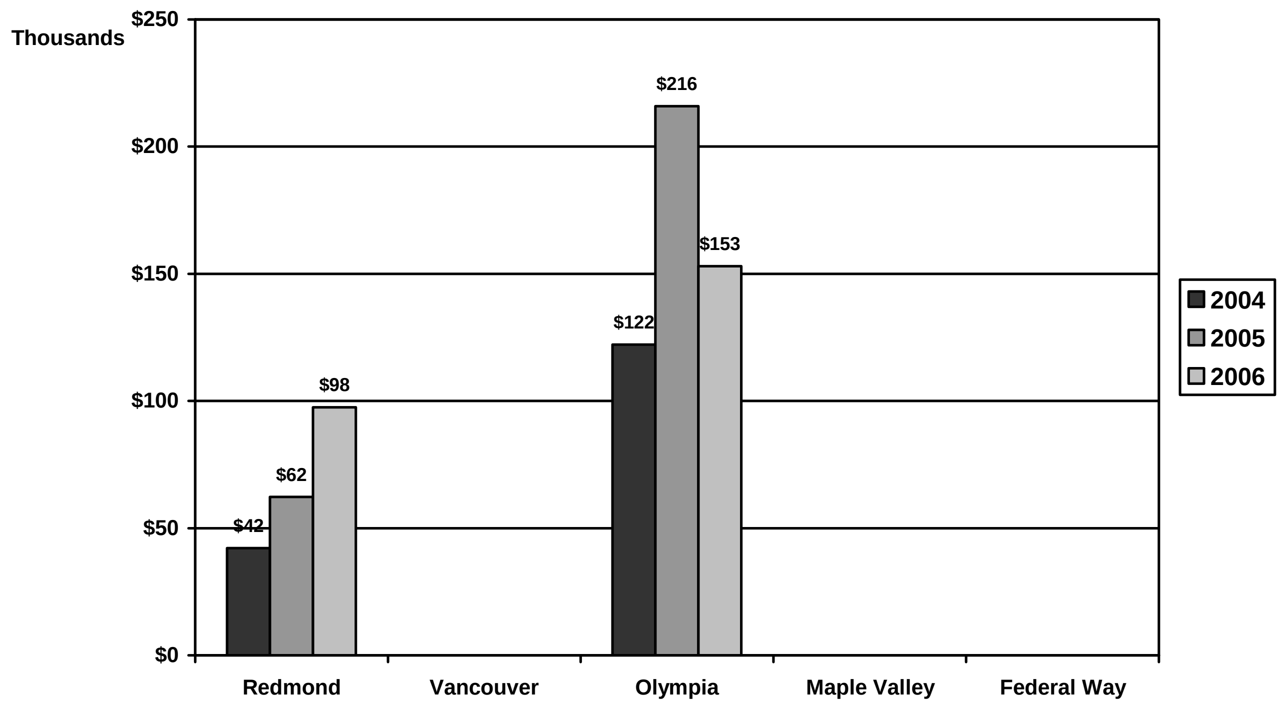
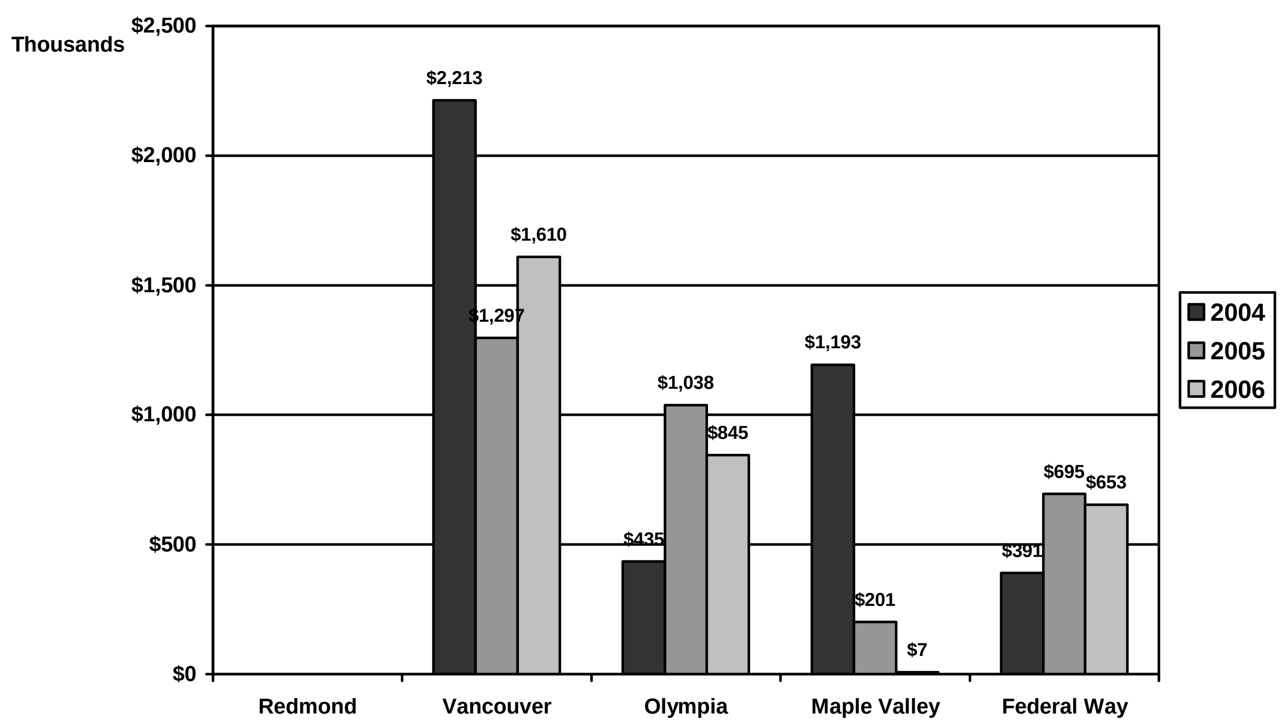


EXHIBIT 4: SCHOOL IMPACT FEES COLLECTED 2004–2006



AUDIT AREA 1 – CAPITAL FACILITIES

FINDING

Washington State law RCW 82.02.050 states that impact fees "may be collected and spent only for public facilities defined in RCW 82.02.090 which are addressed by a capital facilities plan element of a comprehensive land use plan." RCW 82.02.090 provides the following definition of a public facility:

". . . the following capital facilities owned or operated by government entities: (a) Public streets and roads; (b) publicly owned parks, open space, and recreation facilities; (c) school facilities; and (d) fire protection facilities in jurisdictions that are not part of a fire district."

RCW 82.02.090 defines the term capital facilities for fire, transportation, park, and school impact fees. However, the definitions provided are ambiguous, resulting in the Cities applying varying interpretations of the definition of a "fire protection facility."

BACKGROUND

Original Finding Identification

During Phase 1 of the performance audit, Ernst & Young noted that the City of Redmond had spent fire impact fees in the amount of $551,709 to purchase a new fire truck for the downtown Redmond fire station. In looking at the definition of a public facility as defined in RCW 82.02.090, fire impact fees can be spent on "fire protection facilities in jurisdictions that are not part of a fire district," Ernst & Young noted that a fire truck may not fall within the definition of "fire protection facility" in the RCW.

Audit Work Conducted

<u>Clarification of Capital Facilities with the Assistant Attorney General</u>

During Phase 3 of the performance audit, Ernst & Young sought more clarification on the definition of a fire protection facility in regard to RCW 82.02.090. First, Ernst & Young met with the assistant attorney general (AAG) who represents the State Auditor's Office to discuss the definition of capital facilities in the context of fire impact fees. The AAG is a representative of the Washington Attorney General's Office. The AAG informed Ernst & Young that the same question was asked in October 1999 and February and May 2002.

In October 1999 and February 2002, the question was asked of the Municipal Research and Services Center (MRSC).[1] MRSC is a nonprofit organization that provides professional consultation, research, and information services to cities and counties in Washington State. MRSC provided guidance to the inquiring cities that fire apparatus (e.g., fire trucks, etc.) is included in the definition of a capital facility. MRSC's reasoning for providing this guidance included two items:

1. MRSC had researched other Washington State cities' ordinances and code sections. It found three cities where the ordinance or code section indicated that fire impact fees could be spent on fire apparatus.
2. MRSC had consulted with the Washington State Auditor's Office, where the State Auditor's Office provided guidance suggesting that fire apparatus would be included in the definition of fire protection facility.

In May 2002, the same question was asked of the Washington State Auditor's Office. The State Auditor's Office provided guidance to the questioning individual that indicated fire apparatus appears to fall within the statutory usage of the term "fire protection facilities." This decision was based on previous discussions and guidance provided to MRSC.

Ernst & Young noted that municipalities had sought guidance from MRSC and State Auditor's Office because of the absence of guidance from case law, Attorney General Opinions (AGO), or Growth Management Board Decisions. For this reason, Ernst & Young conducted its own research to gain a better understanding of the definition of a capital facility. Ernst & Young researched other Washington State RCWs, the pronouncements of the Government Accounting Standards Board (GASB), and the Financial Accounting Standards Board (FASB), and other states' laws.

Upon conclusion of the research, Ernst & Young noted that RCW 36.70A.070 contains a different description of "capital facilities". Since impact fees are related to the Growth Management Act, it is possible that the Legislature intended RCW 36.70A.070 to limit impact fees.

<u>Growth Management Act – Capital Facility Definition</u>

RCW 36.70A.070 is derived from the Growth Management Act and discusses the mandatory elements of a comprehensive plan. One required element of a city's comprehensive plan is a

capital facilities plan. The following is an excerpt from RCW 36.70A.070(3), which discusses the capital facilities plan element:

"A capital facilities plan element consisting of: (a) An inventory of existing capital facilities owned by public entities, **showing the locations** [emphasis added] and capacities of the capital facilities; (b) a forecast of the future needs for such capital facilities; (c) **the proposed locations and capacities of expanded or new capital facilities** [emphasis added]; (d) at least a six-year plan that will finance such capital facilities within projected funding capacities and clearly identifies sources of public money for such purposes; and (e) a requirement to reassess the land use element if probable funding falls short of meeting existing needs and to ensure that the land use element, capital facilities plan element, and financing plan within the capital facilities plan element are coordinated and consistent. Park and recreation facilities shall be included in the capital facilities plan element."

In looking at the above capital facilities plan element in regard to impact fees, Ernst & Young noted that RCW 82.02.050 states that impact fees "may be collected and spent only for public facilities defined in RCW 82.02.090 which are addressed by a capital facilities plan element of a comprehensive land use plan." Therefore, impact fees can only be spent on capital facilities that are part of the capital facilities plan element. RCW 36.70A.070(3) (as shown above) states that the capital facilities plan must show the locations of capital facilities and the proposed locations and capacities of the new capital facilities. With that said, a fire truck is a moving facility, thus making it difficult to show the proposed location of the fire truck, as required by RCW 36.70A.070. In addition, the capacity of the fire truck must be stated in the plan, raising the question, "What is the capacity of a fire truck?" Therefore, it remains unclear whether spending fire impact fees to purchase a fire truck is in violation of RCW 82.02.050.

Additional Ambiguity with RCW 82.02.050

Ernst & Young noted that there is additional ambiguity in regard to the definition of a capital facility in RCW 82.02.090. In addition to fire impact fees, the following items of the RCW were identified as ambiguous by various cities and Ernst & Young:

1. "Public Streets and Roads": Does this include the entire road system, including items such as sidewalks, or does this mean a road only?
2. "School Facilities": If a fire truck is considered a capital facility, does that mean a school bus is considered a capital facility?

3. Transportation Impact Fee: Can transportation impact fees be spent on all modes of transportation (e.g., biking, walking, metropolitan transit systems) or just roads (i.e., motorized transportation)?

Ernst & Young noted that some of the Cities are conservative in interpreting the definition of a capital facility, while others are more liberal with their interpretation. The conservative Cities are fearful of lawsuits arising if they spend transportation impact fees on items such as biking trails or sidewalks, and therefore they do not use impact fees for these types of transportation facilities. Other Cities have decided to interpret the definition to include multi-modal transportation and are spending impact fees on facilities that the other Cities are not, thus creating an inconsistency across Washington State with regards to the type of facilities funded with impact fees.

RECOMMENDATION

Based on the information provided above, Ernst & Young recommends that the State of Washington amend RCW 82.02.090 to better define capital facilities and alleviate the ambiguity. The amended RCW should better define the following items:

1. Items included in the term “fire protection facilities”
2. Items included in the term “public streets and roads”
3. Items included in the term “school facilities”
4. Address the question of whether transportation impact fees can be spent on multi-modal transportation (i.e., biking, walking, etc.).

Consideration should be given to expanding the definition of capital facilities, not limiting the definition. For example, if clarification were to be given in the RCW that limited “fire protection facilities” to include only fire stations, then the Cities would have trouble spending the fire impact fees collected within the six-year time period that is required by the RCW, as fire stations are generally not built every six years. Therefore, consideration of the definition of capital facilities should be expanded to include items such as fire apparatus (e.g., fire trucks, rescue units, etc.), as the need for more fire apparatus is generally due to growth. In general, consideration should be given to the language of the RCW to make it clear that impact fees can be spent on capital facilities that are necessary to serve new growth.

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There is no true potential cost savings associated with this finding and recommendation, as the RCW remains unclear as to whether or not spending fire impact fees to purchase a fire truck was in compliance with RCW 82.02.050. However, Ernst & Young calculated the dollar value of impact fees spent on questionable uses.

First, Ernst & Young obtained fire impact fee expenditure information from both the City of Redmond and the City of Olympia (the only two Cities that collect fire impact fees) for the performance audit period 2004–2006. The City of Olympia did not spend impact fees on fire apparatus during the performance audit period. However, the City of Redmond spent $551,709 during the performance audit period to purchase a fire truck, as can be seen below in Exhibit 5.

Exhibit 5 – Fire Impact Fee Expenditures for Fire Apparatus for 2004-2006.

Year	Redmond	Olympia	2004–2006 Total
2004	$551,709	$ 0	**$551,709**
2005	0	0	
2006	0	0	

Ernst & Young noted that although the City of Olympia did not spend impact fees on fire apparatus during the performance audit period, that its fire impact fee calculation includes fire apparatus. Under the same guidelines as the fire truck expenditure disclosed above for the City of Redmond, the use of fire apparatus as components of a fire impact fee calculation should be reviewed.

Next, Ernst & Young obtained an estimate of impact fee expenditures spent on alternative modes of transportation during the audit period 2004–2006. The City of Maple Valley is the only city to consider alternative modes of transportation in its transportation impact fee calculation. Over the course of the audit period, it is estimated that the City of Maple Valley spent approximately $325,000 of transportation impact fees on alternative modes of transportation. The City of Maple Valley included these estimated expenditures in its transportation impact fee calculation and therefore collected transportation impact fees specifically for these alternative modes of transportation.

Exhibit 6 – Total Impact Fees Spent on Capital Facilities in Question During 2004–2006.

Audit Period	Fire Apparatus	Alternative Modes of Transportation	Total
2004–2006	$551,709	$325,000	**$876,709**

AUDIT AREA 2 – FIRE DISTRICTS

FINDING

The City of Redmond Fire Department has developed a leading practice in its relationship with King County Fire District No. 34, specifically the method it utilizes to allocate costs of new capital facilities between the City and Fire District 34.

BACKGROUND

Original Finding Identification

According to Washington State law (RCW 82.02.090), fire impact fees can only be collected and spent for "fire protection facilities in jurisdictions that are not part of a fire district." During Phase 1 of the performance audit, Ernst & Young noted that the City of Redmond contracts with King County Fire District No. 34 (the District) to provide fire and rescue services for the entire District. Ernst & Young questioned whether or not fire impact fees were spent on fire protection facilities for the District, a violation of RCW 82.02.090. Therefore, Ernst & Young pursued this question further in Phase 3 of the performance audit.

Audit Work Conducted

During Phase 3 of the performance audit, Ernst & Young conducted further research with the City of Redmond on the potential finding. Ernst & Young noted that the City of Redmond currently has a signed contract in place with Fire District 34 to provide fire and aid services to the District. The City of Redmond provides all fire and aid services to the District, so the District does not need to develop its own fire and rescue services. The contract commenced on September 2, 2004 and terminates on December 31, 2010. The purpose of the contract is to set out terms of service for the following related fire activities

- Establishment of fire prevention
- Education
- Suppression
- Emergency medical care services.

The section of the contract that is of particular importance to the impact fees performance audit is "Section IX – Financing." Section IX discusses how the various expenses of the fire activities will be financed. There are several expense categories, but the following two categories can be funded with impact fees and were therefore important to this particular performance audit:

1. "Suppression, Ambulance, and Facilities: The cost for each station shall be determined based on staffing levels (Attachment B, Page 4). One-half of the cost of each station shall be fully allocated to the jurisdiction where the station is located. The remaining half shall be divided between the City and the District based on the percentage of calls for service that each jurisdiction receives from that particular station. Provided that when no historical data exists, such as for station changes (openings and closures), cost contributions shall be based on projected run data developed by the Fire Department."
2. "Capital Improvement Program: Each project shall be allocated based on project location and benefit, and allocations shall be determined on a project-by-project basis, provided however that projects and estimated costs shall be approved by each jurisdiction prior to being added to the Capital Improvement Program . . ."

Ernst & Young noted that the City of Redmond's current agreement with the District appears reasonable, as the allocation of costs takes into account the number of fire and aid calls from the District versus the City of Redmond. Therefore, according to the calculation discussed above, the City of Redmond can use impact fees for new capital facilities due to growth, up to its proportionate share of the costs (as determined by the calculation above).

<u>City of Redmond/Fire District 34 Contract before September 2, 2004</u>

Prior to the above contract, the City of Redmond and the District were operating under a different agreement. That agreement commenced on December 31, 2000 and terminated the day the above contract was entered into (September 2, 2004). The allocation of fire expenditures between the City of Redmond and the District was different under that contract. Under that contract, the costs were divided among the two parties based on their proportion of the total assessed value for property tax purposes.

This older contract did not appear to allocate costs on a reasonable basis, as it did not take into account the number of calls each fire station receives. The new contract (discussed above) appears to be a leading practice in that it takes into account the number of fire and aid calls from each party in determining their proportionate share of costs for a new public facility.

<u>City of Redmond Fire Impact Fee Expenditures</u>

During the performance audit period of 2004–2006, Ernst & Young noted that only one fire impact fee expenditure occurred in the City of Redmond. In March 2004, an aerial ladder truck was purchased using $551,708.78 of impact fees. The total cost of the truck was roughly $762,700. This purchase was made under the old contract with the District and therefore did not take into account the number of fire and aid calls in determining the proportionate share of costs.

Other Cities' Fire Impact Fees in Relation to Fire Districts

The City of Olympia is the only other city within the scope of the audit that collects fire impact fees. The City of Olympia currently does not provide services to neighboring fire districts like the City of Redmond.

RECOMMENDATION

The City of Redmond has developed a leading practice in its relationship with Fire District 34, specifically the allocation of the proportionate share of expenses between the City and the Fire District. Other cities within the State of Washington should be aware of this leading practice and attempt to implement a similar contract if the city has a relationship with a neighboring fire district.

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There are no potential cost savings associated with this finding and recommendation. However, there is a benefit to implementing the recommendation:

- A more accurate allocation of costs between a city and related fire districts.

AUDIT AREA 3 – PARK ZONING

FINDING

The use of multiple zones is seen as an effective way to reasonably relate the collection and expenditures of park impact fees to areas experiencing growth as discussed at the end of this page. Based on the use of one zone, the City of Olympia is potentially spending neighborhood park impact fees that are inconsistent with its definition of a neighborhood park and results of a citizen survey. Therefore, the City of Olympia may not be spending park impact fees as effectively as it could using multiple zones.

BACKGROUND

Original Finding Identification

During Phase 1 of the performance audit, Ernst & Young noted that the City of Olympia and the City of Redmond use only one zone for the assessment, collection, and expenditure of park impact fees. The City of Vancouver uses multiple park zones in an effort to demonstrate a reasonable relationship between the fee charged to the developer and the park needs generated by growth in that zoning area.

According to RCW 82.02.050 3 (a), impact fees "Shall only be imposed for system improvements that are reasonably related to the new development." While there are no requirements in Washington State law to have multiple park zones, Ernst & Young noted that other cities find zoning to be an effective way to make the impact fee relationship, a reasonable relationship.

Audit Work Conducted

During Phase 3 of the audit, Ernst & Young examined the potential finding further. First, Ernst & Young met with the City of Vancouver to gain an understanding of how multiple park zones work for Vancouver. Next, Ernst & Young met with the City Olympia to gain an understanding of why one zone was selected for assessing, collecting, and spending park impact fees in Olympia. Finally, Ernst & Young sampled some park impact fees that were collected to determine where they were potentially spent within the City of Olympia.

Vancouver's Rationale for Multiple Park Zones

Ernst & Young noted that the City of Vancouver has chosen to implement ten different park zones (or districts) so as to provide a clear demonstration between where fees are spent and where fees are collected. The size of each zone is large enough so that an adequate amount of funding can be collected in each area. The ten park zones span the urban unincorporated area of the county, as the City of Vancouver and Clark County operate under the same parks department. If one were to look at the city limits of Vancouver, there would be approximately four park zones within the City limits. In addition to multiple zones effectively demonstrating the connection between where fees are spent and where they are collected, the City offered the following other benefits of having multiple park zones:

- The impact fees assessed vary by zone to account for the differences in land value across the city. Therefore, a developer building a house in zone one, where land is more expensive, will pay a higher impact fee, where as a developer building a home in zone ten, where land is cheaper, will pay a smaller impact fee.
- Multiple park zones allow the City to have the ability to not collect impact fees in a zone if the zone at some point contains all necessary parks to meet the level of service standards and there is not significant anticipated growth in the zone.

The City of Vancouver did provide some disadvantages to having multiple park zones, which included the following:

- Accounting is more difficult with multiple park zones.
- There is less flexibility with spending the park impact fees collected.
- Spending the impact fees within the six-year time period (as required by law) is more difficult.

City of Olympia One Zone Research

Ernst & Young met with the City of Olympia to gain an understanding of how one park zone works for the City and how effectively the single zone demonstrates the connection between where fees are collected and where they are spent. Ernst & Young noted that because the City operates its parks system as a single zone, Olympia may spend park impact fees collected in the City on any park within the City limits.

Types of Parks in Olympia

First, Ernst & Young noted that the City of Olympia develops the following types of parks using park impact fees, as per the City's Capital Facilities Plan[9]:

- Neighborhood Parks: Neighborhood parks are a common gathering place for families and children, all within a 10–20 minute walk from home.
- Community Parks: Community parks are places for organized recreation programs and sports activities. Community parks will include athletic fields and picnic shelters or other facilities for large-scale community use.
- Special Use Parks: Special use parks offer unique features and are typically more special-interest oriented. Examples of these parks are the Japanese Garden and Heritage Fountain. These parks are used by the entire community and become treasured places in the community.
- Open Space Parks: Open space is for passive use, nature trails, and wildlife habitat.

Questions Regarding the Neighborhood Park Designation

After gaining an understanding of the various types of parks, Ernst & Young became concerned about the neighborhood park designation. All other parks (community, special use, and open space) in the City of Olympia are built for use by the entire City (as per their definition shown above); thus, implementation of a single park zone appears reasonable, as the entire community benefits from the development of these parks regardless of where a home is built. However, neighborhood parks are built specifically for neighborhoods, as the definition in Olympia's capital facility plan indicates that they are a 10–20 minute walk from a home. Furthermore, Olympia's Park and Open Space Standards and Definitions document[3] describes neighborhood parks as ". . . generally small in size and serve an area of approximately one-half to one mile radius but serve all residents in the community." Based on this understanding, Ernst & Young noted that one park zone might allow a park impact fee to be collected on one side of the City, yet be spent on building a neighborhood park across town, outside of the City's own definition of neighborhood parks. In this scenario, the neighborhood park may not benefit the citizens and developers who paid the park impact fee, as the neighborhood park is built further than a 10–20 minute walk and further than one-half to one mile away.

The City of Olympia's Justification for One Zone

The City of Olympia implemented park impact fees in 1993 and has utilized one zone since its implementation. The justification for the City's determination to use one zone in 1993 is based on reasoning similar to that identified by the City of Vancouver as disadvantageous to having multiple park zones (noted above). The City of Olympia further explained to Ernst & Young that the "reasonableness" of one zone can be understood based on the outcome of an Olympia citywide survey conducted in 2006.[4] The survey was conducted by the City to assess residents' opinions and behaviors regarding City services. The survey included the following City government programs and services:

- Communication with citizens
- Garbage and recycling
- Sewer
- Drinking water
- Storm and surface water
- Parks
- Public safety
- Transportation services

The survey selected 400 residents, at random, from a list of utility customers. The survey was conducted over the phone and has a margin of error of +/- 5% at the 95% confidence interval. The direct results of the parks portion of the survey included the following:

- "39% visited a park in Olympia 12 or more times in the past year.
- 7 in 10 were "very satisfied" with their park experiences.
- Majorities were "definitely" willing to travel up to six miles to get to an open space area (59%) and a special use park (52%); 44% were "definitely" willing to travel to a community park.
- 3 in 5 were "definitely" (36%) or "probably" (25%) willing to travel three miles to a neighborhood park.
- 1 in 3 respondents (or someone in their household) had participated in a recreational activity provided by the City.
- 9 in 10 agreed that art events are valuable to the quality of life in the City."[4]

Ernst & Young's Views on the Survey Results

The survey results for the special use, open space, and community parks (bullet three above) do support the City's definition and plan for usage of these parks by citizens across the City in a single park zone. However, the survey results (bullet four above) do not support the City's definition and/or implementation of a single park zone for neighborhood parks. The survey shows that a total of 61% of Olympia residents would "definitely" or "probably" travel up to three miles to visit a neighborhood park. The City of Olympia is approximately six miles across; therefore, survey results for neighborhood parks do not correlate to the City's approach of one zone.

Testing of Park Impact Fees Collected

Ernst & Young conducted an analysis of park impact fee collections during the audit period 2004 – 2006 and the expenditure of the 2004 and 2005 collections. . Ernst & Young found that although there were community, special use, or open space park systems located close to where the impact fees were gathered, roughly 96% of the neighborhood parks were not built within the one-half to one mile radius of where the impact fees were gathered. Ernst & Young also found that the average distance between the location where an impact fee was collected and the location where the impact fee was potentially used (the average distance of the impact fee collection to the three possible parks where the impact fee was spent) on a neighborhood park was approximately four and one-half miles. This four and one-half mile average shows that neighborhood parks are not built within the one-half to one mile radius or 10 to 20-minute walking distance from the location of the development, based on Olympia's definition of neighborhood parks. Given that neighborhood parks are constructed at locations that on average may be several miles from the impact fee collection development site, neighborhood parks are being developed in current neighborhoods lacking parks, raising the question of whether the single zone approach most effectively demonstrates the connection between the impact fees and the growth that paid them.

System Approach to Parks in Olympia

To support its neighborhood park definition, City planners in Olympia explained the one-half to one mile distance is a goal for the City's system of parks. This goal is based on a standard level of service of neighborhood park acres for 1,000 residents. Olympia has a goal of 1.44 acres per 1,000 residents. Olympia utilizes a 20-year plan for its parks system. In the next 20 years, the City hopes to realize its current definition of a neighborhood park.

Olympia explained to Ernst & Young that its park planning utilizes a "systems approach." According to RCW 82.02.050 3(c), Impact fees are permitted to be "used for system improvements that will reasonably benefit the new development." Olympia's parks may be considered appropriate improvements given the definition of *System Improvements* in RCW

82.02.090: "public facilities that are included in the capital facilities plan and are designed to provide service to service areas within the community at large, in contrast to project improvements."

RECOMMENDATIONS

Cities should consider the use of multiple zones to more effectively demonstrate a clear relationship between where impact fees are collected and spent. Ernst & Young recommends that the City of Olympia take both of the following actions in its approach to park planning:

1. Consider revising the "one-half to one mile" and "10–20 minute walk" statements from its definition of a "Neighborhood Park" if the City's intent is to build these neighborhood parks for the entire City rather than for a more localized neighborhood.

2. Consider dividing the City into two park zones to more effectively demonstrate a clear relationship between where impact fees are collected and spent. Two zones for park impact fees would appear to be reasonable, as the City is approximately six miles across and according to the survey:

   "3 in 5 were "definitely" (36%) or "probably" (25%) willing to travel three miles to a neighborhood park."

   If 61% of the citizens are "definitely" or "probably" willing to travel three miles to a neighborhood park, then dividing the City into 2, three-mile wide zones would appear to be appropriate to meet the demands of the City residents.

Note: The City of Redmond uses only one park zone as well; however, the audit focused on the City of Olympia because it exhibited the greatest opportunity during the Phase 1 planning process. No detailed performance audit work was conducted at the City of Redmond; however, the City of Redmond should consider the above recommendations as well.

POTENTIAL COST SAVINGS AND/OR OTHER IMPACTS

There is no direct potential cost savings associated with the recommendations above. However, with the current definition of a neighborhood park, Ernst & Young calculated the dollar amount of impact fees that were collected during the performance audit period (2004–2006) that were potentially spent more than three miles away (Note: Ernst & Young used three miles, rather than one-half to one mile, due to the results of the survey discussed above). This dollar figure was calculated by performing the following steps:

1. Randomly selected a sample of 50 neighborhood park impact fees collected during the period (12% of the entire population). A total of 417 neighborhood park impact fees collected during the performance audit period have been expended.
2. Determined the distance between the address where the impact fee was collected and where the impact fee could have potentially been spent within the City on a neighborhood park. Ernst & Young used Google Maps to perform this function.
3. Out of 50 samples selected, Ernst & Young noted that 80% of impact fees were potentially spent on a neighborhood park more than three miles away.
4. Ernst & Young then extrapolated the results of the testing to the remaining 417 impact fees collected for the period by determining that 80% of the entire amount was potentially spent on neighborhood parks greater than three miles away. The total dollar figure came to $36,974.
5. Finally, Ernst & Young noted that park impact fees have been collected in the City of Olympia since 1993 under the same methods and park definitions. However, Ernst & Young did not obtain data outside of the performance audit period (i.e., outside the scope of the audit) and was therefore unable to calculate the total dollar amount of park impact fees spent on neighborhood parks in areas that did not experience growth since the inception of the fee in 1993.

   Refer to *Appendix E – Olympia Park Impact Fee Collection and Spending* for a detailed map of the sample of 50 park impact fees tested.

Exhibit 7 – Estimated Olympia Park Impact Fees Potentially Spent on Neighborhood Parks Greater Than Three Miles Away During the Performance Audit Period of 2004-2006

	2004–2006
Estimated Olympia Park Impact Fees Potentially Spent on Neighborhood Parks Greater Than Three Miles Away	$36,974

AUDIT AREA 4 – INTEREST-BEARING ACCOUNTS

FINDING

Impact fee receipts are retained in separate general ledger (GL) accounts, not in separate interest-bearing bank accounts. The impact fees are usually invested with the rest of a city's cash in a variety of investments. At the end of the month, interest earned on these investments is allocated back to the GL accounts. We noted that the interest allocation method used by each city is different. Additionally, we noted the City of Vancouver's treasury management as a leading practice in tracking investments and appropriately allocating interest to impact fees.

BACKGROUND

Original Issue Identification

As part of Phase 1 of the performance audit, Ernst & Young noted that the Cities maintain separate GL accounts for each impact fee type collected; however, the impact fees are invested in the citywide bank account. Monies in the citywide bank account are then invested by the treasury departments in each city. Interest earnings on these investments are allocated to the GL accounts at the end of each month.

The treatment of impact fee receipts by the Cities differed from our understanding of the Washington State statute RCW 82.02.070:

> *"(1) Impact fee receipts shall be earmarked specifically and retained in special interest-bearing accounts. Separate accounts shall be established for each type of public facility for which impact fees are collected. All interest shall be retained in the account and expended for the purpose or purposes for which the impact fees were imposed."*

Language referencing "separation of accounts" and "retaining" rather than "allocating interest" initially led us to interpret the RCW as requiring separate interest-bearing bank accounts, beyond GL accounts, for each type of impact fee collected.

Audit Work Conducted

<u>Clarification of Interest-Bearing Accounts with the Assistant Attorney General</u>

During Phase 3 of the performance audit, Ernst & Young sought more clarification on the interpretation of RCW 82.02.070. First, Ernst & Young met with the AAG who represents the State Auditor's Office to discuss our questions regarding the RCW. The AAG's office located guidance on our question in the Budgeting and Accounting Reporting System (BARS) manual produced by the Washington State Auditor's Office. The BARS manual, Chapter 1, reads: "The Washington State Auditor's Office prescribes the accounting and reporting of local governments in the State of Washington, under RCW 43.09.200. This prescription is performed using Budgetary, Accounting, and Reporting System (BARS) manuals and financial reporting packages."

The BARS manual specifies account number 345.85 as the account in which impact fee receipts should be recorded. This is an "account" in terms of a GL account, and not a separate bank account. Interest should be allocated to this account each month based on the interest that is earned. Therefore, according to the BARS manual, Ernst & Young now concludes that impact fees do not need to be retained in a separate interest-bearing bank account.

<u>Change of Focus</u>

In a follow-up meeting with the State Auditor's Office, Ernst & Young and the State Auditor's Office determined that as the Cities already segregate impact fees into separate GL accounts per the BARS manual, the performance audit of the original issue would change focus, and Ernst & Young would focus its efforts on the appropriate allocation of interest earned on investments to those accounts in the Cities. Ernst & Young selected the following Cities to look at interest allocation methods:

1. City of Vancouver
2. City of Redmond
3. City of Olympia
4. City of Maple Valley

<u>Interest Allocation Methods of Each City</u>

City of Vancouver

The City of Vancouver uses the Emphasys SymPro system (SymPro) to assist in managing the City treasury function, including the interest allocation. SymPro tracks investment earnings and interfaces with the City's GL to retrieve the daily balances for all accounts to which to allocate interest. Investment earnings are then allocated across the GL accounts based on their average daily balances.

The average daily balance is calculated by determining the balance of the account at the end of each day of the month and finding the arithmetic mean of those balances. The arithmetic mean is then used as the allocation base between GL accounts. The SymPro system multiplies each deposit to the account by the number of days that balance was on deposit to find a total number of "dollar days" per account and prorates total earnings by the number of dollar days for each account relative to the sum of dollar days for all accounts.

City of Redmond

The City of Redmond allocates interest to a fund containing all types of impact fees based on the average weekly balance of all funds, and then uses a spreadsheet to allocate interest to the various impact fee types within the fund at month-end based on the average of the beginning and ending balances of each fee account. Instead of allocating actual interest earnings across average daily balances within the spreadsheet, the City of Redmond allocates interest based on the Washington State Local Government Investment Pool (LGIP) rate based on the ending balances in impact fee accounts. The LGIP is an investment fund managed by the State of Washington Treasurer to serve as an investment vehicle for local governments. Therefore, the City of Redmond is not allocating the total dollar amount of interest that is actually earned; rather, it is using the LGIP, which is close to the rate of return, but not 100% accurate. A journal entry is booked to record the interest earned on impact fees. The journal entry reduces interest earned from the general fund and places the interest in the impact fee accounts.

City of Olympia

The City of Olympia has a pooled cash function within its accounting system where it tracks its investments. Interest earnings on investments, as well as interest on the City's checking account, are allocated using a pooled cash program that allocates earnings based on average daily balances of the funds throughout the month. The City maintains one fund for all impact fee types in its primary accounting system. The City uses an Excel worksheet independent from the system to track separate impact fees for different services (i.e., fire, park and transportation). Interest allocated to the impact fee fund is subsequently allocated between impact fee types within the Excel worksheet based on the fee account balances at month-end.

City of Maple Valley

Maple Valley allocates interest to the school impact fees collected using the most recently published monthly earnings rate from the Washington LGIP, managed within the Washington

State Treasurer. The LGIP rate is applied to each fee for the number of days from receipt by the City to the check being issued to the school district. Remaining actual interest earnings are prorated to other funds, including Transportation Impact Fees, based on the average of beginning and ending fund balances.

The City of Maple Valley feels using the LGIP rate to allocate interest to school impact fees is a more accurate interest rate than using a rate from all its combined investments (including long-term investments). School impact fees are only retained in the account for 30–45 days before they are remitted to the school districts (refer to *Audit Area 5 – School Impact Fee Interest* for more information regarding school impact fees). Therefore, using the LGIP rate, which is a short-term investment rate, is more accurate, as the City is only holding the school impact fees for a short period of time.

RECOMMENDATIONS

There are two recommendations associated with this finding:

1. Cities should maintain each impact fee type in its own fund or GL account and allocate actual interest earned on cash investments based on the relative average daily balances, similar to the City of Vancouver, as described above. The Cities should consider procuring technology, which allows for a daily allocation of interest and minimal manual input.

   Cities should not allocate interest based on an interest rate that is not equal to actual interest earned. Redmond and Maple Valley allocate interest to impact fees based on the LGIP rate, even though this will not be the same as their actual earning rate when all city cash is not maintained in the LGIP. One exception to this recommendation would be the school impact fee interest allocation. Since school impact fees are only held for a short period of time, using the LGIP would make sense – however, <u>only</u> for school impact fees.

2. Washington State should consider modifying RCW 82.02.070 to better define “separate interest-bearing accounts.”

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There are no potential cost savings associated with this finding and recommendation. However, there are benefits to implementing the recommendation:

Recommendation 1:

- Automation of interest allocation may reduce required accounting staff time.
- Accurate interest allocation prevents acceptance of unsupported excesses or deficiencies in interest earnings accounts that could make these accounts prone to errors or fraud.

Recommendation 2:

- Current language in the RCW can be understood to mean that impact fees must be maintained in separate bank accounts. We note that maintaining impact fees in a pooled cash account with accurate interest allocation to the fees facilitates cash management practices.
- Amending the RCW to clearly define “separate interest-bearing accounts” will alleviate the ambiguity that the current RCW language creates.

AUDIT AREA 5 – SCHOOL IMPACT FEE INTEREST

FINDING

RCW 82.02.070 requires that "Impact fee receipts shall be earmarked specifically and retained in special interest-bearing accounts. Separate accounts shall be established for each type of public facility for which impact fees are collected. All interest shall be retained in the account and expended for the purpose or purposes for which the impact fees were imposed."

Ernst & Young noted that while school impact fees are in the custody of the city, they earn interest because they are deposited in the city's pooled cash bank account and are invested along with other city funds. The cities of Maple Valley and Vancouver remit interest earned between the time the fees are received by the city and the time they are remitted to the school district. The cities of Olympia and Federal Way do not remit any interest to the school districts, so the interest earned during this time does not appear to be expended for the purpose for which the impact fee was imposed, as required by RCW 82.02.070.

BACKGROUND

Original Finding Identification

As part of Phase 1 of the performance audit, Ernst & Young noted that the school districts determine the impact fee amount to be charged, and the Cities collect the fee through the permitting process on behalf of the school districts. (Refer *to Audit Area 7 – School Impact Fees* for more information regarding the school impact fee process and the relationship between the school districts and the Cities.) The city records the impact fees received as a liability and remits the monies to the school district at the beginning of each month for the fees collected in the previous month. The monies collected by the city are invested along with other city cash; however, the interest earned on the investment of the school impact fees is not remitted to the school districts in the cities of Olympia or Federal Way.

We noted that the interest earnings on the school impact fees while they are in the custody of the city are not remitted to the school districts and therefore may not be expended for the purpose for which the impact fees were imposed, as required by RCW 82.02.070: "Impact fee receipts shall be earmarked specifically and retained in special interest-bearing accounts. Separate accounts shall be established for each type of public facility for which impact fees are collected. **All interest shall be retained in the account and expended for the purpose or**

<u>purposes for which the impact fees were imposed</u> [emphasis added].” The interest earned on school impact fees should be spent on school capital facilities, since the impact fees were imposed for schools.

Additionally, during Phase 1 of the performance audit, Ernst & Young noted that the City of Vancouver tracks school impact fees collected on behalf of the school districts, books a liability to record the amount owed, and distributes the monies to the appropriate school district by the 10^{th} of the following month, including interest earned. It was noted that the City of Vancouver has not always remitted the school impact fee interest. In 2005, Vancouver became aware of this mistake and remediated the issue. The City of Vancouver paid the school districts all interest owed from the inception of the school impact fees and continues to remit the interest earned each month.

Audit Work Conducted

During Phase 3 of the performance audit, Ernst & Young further researched and investigated the finding. Ernst & Young reviewed actual school impact fee data, which showed the amounts collected and remitted for the performance audit period (2004–2006) from the cities of Vancouver, Maple Valley, Olympia, and Federal Way. The City of Redmond did not collect school impact fees during the performance audit period, and therefore no data was collected from Redmond. In reviewing the data obtained, Ernst & Young noted the following differences between the Cities in how they remit interest to the school district:

- Vancouver allocates interest to school impact fees based on actual daily interest earnings and the daily balance of the school impact fee account. Ernst & Young noted this as a leading practice in *Audit Area 4 – Interest-Bearing Accounts*.
- Maple Valley allocates interest to fees at the end of the month before they are remitted by allocating the interest that would be earned from the state LGIP for the number of days between receipt of the fee by the City and remittance to the district.
- Olympia and Federal Way do not remit interest to the districts.

Ernst & Young then prepared an estimate of the amount of school impact fee interest that should have been remitted to the school districts during the audit period. This estimate was based on interest allocated to the average daily balance of school impact fee accounts at Olympia and Federal Way and to the ending monthly balance of fees collected for the period from the end of the month until the fees are remitted to the district. To come up with this estimate, Ernst & Young used the same rate as the State of Washington LGIP.

RECOMMENDATION

Ernst & Young recommends that the Cities review and allocate actual interest earnings to school impact fees collected and remit those interest earnings to the appropriate school district(s), so the interest earned on the school impact fees can be expended for the purpose for which the school impact fees were imposed. This is required under RCW 82.02.070 in order for all interest earnings to be expended for the purpose or purposes for which the impact fees were imposed. (For information on how to allocate the interest to the school impact fees, refer to *Audit Area 4 – Interest-Bearing Accounts*.) Furthermore, the City should retroactively determine that interest has been properly allocated.

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There is no direct potential cost savings associated with this finding, but rather a reallocation of resources between the Cities and the local school districts. Ernst & Young estimated the amount of interest that should have potentially been allocated to the school impact fees collected by the cities of Federal Way and Olympia in a two-step process:

1. Calculated average daily balance of school impact fee activity during each month, and allocated one month of interest to the balance based on that month's Washington State LGIP
2. Calculated the number of days the fees were held between month-end and remittance to the district and allocated interest to the amount of the remittance for these days.

Exhibit 8 – Estimated Interest Not Remitted to the School Districts During the Performance Audit Period of 2004-2006

City	Interest During The Month	Interest After Month-End	Total Interest Not Remitted 2004-2006
Olympia	$3,818	$2,411	$6,229
Federal Way	$1,559	$1,681	$3,240
		TOTAL	**$9,469**

This finding is identifiable to the time the school impact fees were first assessed by each city. The City of Olympia first collected its school impact fees in 1993 and the City of Federal Way started in 1996. Time periods outside of 2004-2006 were not in scope for this Ernst & Young performance audit, but should be reviewed and retroactively considered by each City.

AUDIT AREA 6 – FIRE IMPACT FEE SCHEDULE/CALCULATION

FINDING

The City of Redmond has developed a leading practice in its fire impact fee schedule/calculation. Specifically, the schedule/calculation takes into account the impacts of fire and aid calls by land use type, projected growth by land use type and the fire Capital Facilities Plan (CFP).

The City of Olympia's fire impact fee schedule/calculation does not appear to effectively demonstrate the fee's connection to system improvements related to growth, the cost of public facilities necessitated by new development or the availability of other financing.

BACKGROUND

Original Finding Identification

During Phase 1 of the performance audit, Ernst & Young noted that the City of Olympia collects fire impact fees at a flat per-square-foot rate ($0.159 per square foot), regardless of the land use type. Therefore, a single-family home pays the same rate per square foot as a restaurant or manufacturing facility. The fire impact fee rate was determined by an outside consultant in 1994. Ernst & Young noted that the fire impact fee has not been updated since its adoption in 1994.

During Phase 1, Ernst & Young noted that the City of Redmond assesses fire impact fees based on the type of land use. To determine the fire impact fee that each type of land use pays, the City of Redmond takes into consideration the number of historical fire and aid calls based on the type of land use (i.e., multi-family vs. retail, etc.).

Audit Work Conducted

During Phase 3 of the performance audit, Ernst & Young spent more time working with the cities of Redmond and Olympia to gain a better understanding of how the impact fee calculation and schedule were determined.

<u>Fire Impact Fees in the City Olympia</u>

City of Olympia Planning and Fire Department

Ernst & Young met with the City of Olympia's Fire Department and Planning Department to gain a better understanding of the impact fee calculation that what was prepared in 1994 to determine the reasoning behind a flat rate for all land uses. The City of Olympia was initially unable to explain how the calculation was determined in 1994, as there were no individuals currently within the City who were working when the calculation was determined. Further information was later provided by the City to speak to the independent study that was conducted in 1994 to determine the impact fee rate. The information provided explained how the City's approach was standards-driven, using prior years' costs against the total area of fire coverage to define a per-square-foot fee for any new development in the City to maintain that standard level of service. The City maintained that this method allows it to forecast the cost of new fire protection based on prior years' incurred expenses. However, the City did state that this method did not directly relate to its forecasted expenses for fire protection facilities in its capital facilities plan. The City of Olympia also explained to Ernst & Young that there have been very few (if any) developer complaints regarding the fire impact fee requiring a detailed explanation of the study.

Rate Study

Ernst & Young was able to obtain a copy of the fire impact fee study prepared for the City by an independent consultant in 1994[7]. Ernst & Young reviewed the study to gain an understanding of how the calculation was prepared, and the rate was ultimately determined. Ernst & Young noted that the fire impact fee rate per square foot was calculated by the independent consultant using the following steps:

1. Determined the City of Olympia's fire protection facilities inventory as of June 1992 and the 1992 square feet of development served by the current inventory. Using these figures, a fire apparatus per square foot was determined for the City for 1992. See Exhibit 9 below.

Exhibit 9 – Fire Apparatus per Square Foot of Development[7]

Component	Number of Apparatuses	Square Feet of Development Served	Apparatus Per Square Foot
Stations	3	38,171,851	.000000078
Pumpers	6	38,171,851	.000000157
Rescue Units	3	38,171,851	.000000078
Aerial Units	1	38,171,851	.000000026
Hazardous Materials Units	1	38,171,851	.000000026

2. Next, the 1992 cost per inventory item was determined, as well as a cost per square foot. See Exhibit 10 below.

Exhibit 10 – Capital Cost per Square Foot of Development[7]

Component	Apparatus Per Square Foot	Cost Per Apparatus	Capital Cost Per Square Foot
Stations	.000000078	$ 1,684,000	$ .131352
Pumpers	.000000157	275,000	.043175
Rescue Units	.000000078	55,000	.00429
Aerial Units	.000000026	400,000	.0104
Hazardous Materials Units	.000000026	80,000	.00208
Total Cost/Sq Ft			*$ 0.191297*

3. Previous years' expenditures for fire protection facilities were then determined. See Exhibit 11 below.

Exhibit 11 – Previous Expenditures for Fire Protection Facilities[7]

Year	Expenditures
1985	$ 37,870
1986	285,940
1987	137,530
1988	47,120
1989	47,280
1990	42,460
1991	109,780
1992	28,308
1993	36,410
9-Year Total	*$772,698*

4. An annual average of the nine-year total was calculated ($85,855). Using this number, along with the 1992 square feet of development (38,171,851), an annual average per square foot of development was computed: $0.0022491.

5. Using a discount rate of 7%, the net present value of 27.5 years of future payments (at $0.0022491) will total $0.032157 per square foot.
6. Therefore, the impact fee rate is $0.159140 per square foot ($0.191297 (from Exhibit 14) minus $0.032157.))

Upon completion of reviewing Olympia's fire impact fee calculation to arrive at the $0.159 per square foot assessed to developers, Ernst & Young could not determine whether Olympia's rate study meets the following requirements by Washington State law:

- "Should only be imposed for system improvements that are reasonably related to the new development" (RCW 82.02.050). Furthermore, "system improvements" are defined in RCW 82.02.090 as ". . . public facilities that are included in the capital facilities plan and are designed to provide service to service areas within the community at large, in contrast to project improvements."
- "Should not exceed a proportionate share of the costs of system improvements that are reasonably related to the new development" (RCW 82.02.050).
- A schedule of impact fees adopted for each type of development activity subject to impact fees, including (RCW 82.02.060):
  - ➢ The amount of the impact fee to be imposed for each type of system improvement
  - ➢ The schedule should be based on a formula or other calculation method
  - ➢ The formula should take into account proportions including, but not limited to:
    1. The cost of public facilities necessitated by new development
    2. The methods by which public facilities were financed
    3. The availability of other means of funding public facility improvements
    4. An adjustment to the cost of the public facilities for past or future payments either made or anticipated to be made, including payments proratable to the system improvement, along with:
       a. User fees
       b. Debt service payments
       c. Taxes

Ernst & Young noted that the City of Olympia's fire impact fee calculation does not appear to include all required considerations:

1. System improvements that are needed due to growth (a requirement of RCW 82.02.050); rather, the calculation uses previous years' expenditures.
2. Proportionate share of the costs of system improvements related to new development (a requirement of RCW 82.02.050), as no such information related to new development is mentioned in the calculation.
3. The formula used to determine the fire impact fee amount does not appear to take the following items into consideration (a requirement of 82.02.060):
   - The cost of public facilities necessitated by new development
   - The methods by which public facilities have been financed
   - The availability of other means of funding public facility improvements
4. The calculation was conducted in 1994 and has not been revised or updated since implementation, even though costs and growth patterns have changed.
5. The calculation includes capital facilities that are currently ambiguous under RCW 82.02.090. As stated in Audit Area 1 of this report, RCW 82.02.090 defines the term capital facilities for fire, transportation, park and school impact fees. However, the definitions provided are ambiguous, resulting in the Cities applying varying interpretations of the definition of a "fire protection facility." Under the same guidelines as those defined in Audit Area 1 of this report, the City of Olympia's use of fire apparatus (i.e., pumpers, rescue units, aerial units and hazardous materials units) as components to its fire impact fee calculation should be considered.

<u>Fire Impact Fees in the City of Redmond</u>

Next, Ernst & Young met with the City of Redmond to gain an understanding of the formula it used to calculate the City's fire impact fee schedule. Exhibit 12 below shows the City of Redmond's fire impact fee schedule for the performance audit period.

Exhibit 12 – City of Redmond's Fire Impact Fee Schedule 1999-2006

Land Use	Impact Fee
Single-family	$94.48 per residential unit
Multi-family	$132.73 per residential unit
Office	$0.11 per square foot
Retail	$0.13 per square foot
Industrial	$0.01 per square foot

In order to develop the different rates for land use categories as shown above, the City of Redmond used historical data to determine the number of emergency (fire and aid) calls per land use type. Ernst & Young noted that national emergency call data is available; however, it was important for Redmond to use Redmond data instead of national data, given that the jurisdiction has unique fire safety requirements.

The City of Redmond determined its fire impact fee schedule (Exhibit 12) by performing the following calculation steps in 1999:

1. Determined the capital facility needs for the fire department as of 1999. Once the capital facility needs were identified, the City of Redmond determined the percentage of those needs that arose due to growth.
2. Obtained 1997 historical incident response (fire and aid) data from the City fire department. Response data is logged by the City of Redmond according to 13 land use categories. The land use incident response data was further organized into the following land use categories:
   a. Single-family
   b. Multi-family
   c. Office
   d. Retail
   e. Industrial
3. Determined the increase in annual incident responses due to growth, by land use type.
4. Allocated the capital facility needs by incident responses due to growth (calculated in step one above) to each land use type, based on the proportionate number of incident calls per land use type.
5. Calculated the anticipated growth per land use type over a 17-year period.
6. Determine the impact fee to be paid by each land use type (Exhibit 16) by dividing the capital costs allocated to each land use type (step four) by the anticipated growth per land use type (step five).

Ernst & Young noted that the City of Redmond's fire impact fee calculation and schedule met all aspects of RCW 82.02.050 and 82.02.060 and demonstrates a leading practice. Redmond's fire impact fee calculation and schedule takes the following items into consideration:

- System improvements that are reasonably related to growth
- The proportionate share of the costs of system improvements related to new development

Finally, the City of Redmond reviewed its fire impact fee schedule in 2006 and noted that updates were needed. Therefore, the schedule was updated in 2006, and new rates were charged for fire impact fees.

RECOMMENDATION

Other cities within the State of Washington should be aware of the City of Redmond's leading practice for the fire impact fees schedule/calculation.

The City of Olympia should revisit its fire impact fee schedule and consider if it is suitable to continue charging the fire impact fee. Specifically, Olympia should more effectively address RCW 82.02.050 and 82.02.060 in its calculation and demonstrate that the fire impact fee charged reasonably relates to system improvements that are reasonably attributable to growth.

Additionally, the City of Olympia should consider implementing a periodic review of its fire impact fee calculation and schedule to determine that the fee is still adequate, given the yearly changes in growth expectations and capital facility needs.

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There are no direct potential cost savings associated with this finding and recommendation. However, Ernst & Young looked at and compared the City of Olympia's fire impact fee in two ways:

1. Scenario 1: Ernst & Young used the City of Redmond's calculation and growth data to project what the City of Olympia's fire impact fee schedule could have potentially been during the audit period, based on actual costs defined in the City of Olympia's 2003 capital facilities plan.
2. Scenario 2: Ernst & Young took the City of Olympia's current fire impact fee calculation and removed the capital facilities in question (i.e., fire apparatus).

Ernst & Young then took the above two scenarios and compared them to the amount of fire impact fees that were collected during the audit period.

Scenario 1: Fire Impact Fee Schedule Calculation Based on the City of Redmond's Calculation

Ernst & Young used the City of Redmond's calculation, noted as a leading practice in our finding in this audit area, as a way to demonstrate what the City of Olympia's fire impact fee might have been if it was directly tied to its fire CFP. Ernst & Young also used the City of Redmond's growth data and historical statistical fire and aid response data to develop a potential fire impact fee schedule for the City of Olympia. To do this, Ernst & Young performed the following steps:

1. Used the City of Olympia's Fire CFP from 2003 as a basis for the needed capital facilities. (Note: Ernst & Young could not determine the capital facilities in the 2003 CFP that were due to growth; therefore, Ernst & Young used 100% of the fire capital facilities from the plan for purposes of this calculation.)
2. Inserted Olympia's CFP data into Redmond's calculation. Olympia did not have sufficient historical incident response data (determines the fee each land use type pays) or anticipated growth data to use in the calculation. Therefore, for purposes of this calculation, Ernst & Young used Redmond's historical incident response data and Redmond's anticipated growth with the following adjustments. Ernst & Young noted that the City of Redmond is a high-growth city, where as the City of Olympia is somewhat of a low-growth city; therefore, Ernst & Young did not use 100% of the City of Redmond's growth in the calculation for the City of Olympia. Rather, Ernst & Young looked at the population growth between the two cities during the period 2000–2007 and noted that the City of Olympia's growth was 36% of the City of Redmond's growth, based on population statistics. Therefore, Ernst & Young used 36% of Redmond's growth in the calculation and applied this to the growth rates by land use type noted below.

Note: The City of Redmond's anticipated growth over the 17-year period varies by land use type. The information below details the City of Redmond's anticipated growth rate by land use type for the 17-year period and the City of Olympia's estimated growth rate by land use type at 36% of Redmond's anticipated growth.

Land Use Type	City of Redmond's Forecasted Growth	City of Olympia's Estimated Forecasted Growth
Single-family	54%	19%
Multi-family	63%	23%
Office	133%	48%
Retail	65%	23%
Industrial	24%	9%

After performing the above steps, Ernst & Young estimated the potential fire impact fee schedule for the City of Olympia for the performance audit period. Exhibit 13 below shows the potential fire impact fee schedule for the City of Olympia.

Exhibit 13 – Potential Olympia Fire Impact Fee Schedule Based on Anticipated Growth Equal to 36% of Redmond's Anticipated Growth

Land Use	Impact Fee
Single-family	$82.73 per residential unit
Multi-family	$116.22 per residential unit
Office	$97.02 per 1,000 sq. ft.
Retail	$110.99 per 1,000 sq. ft.
Industrial	$11.45 per 1,000 sq. ft.

Next, Ernst & Young obtained a list of all fire impact fees collected for the performance audit period (2004–2006) *(Note: A total of $491,036 in fire impact fees was collected for the period.)* Using this data, Ernst & Young recalculated each fire impact fee collected. Using the above fire impact fee schedule, it shows that the City of Olympia under this scenario would have potentially collected $145,723 in fire impact fees, which is $345,313 less than what the City charged under its current calculation.

Scenario 2: Recalculation of the City of Olympia's Fire Impact Fee Calculation

Ernst & Young used the fire impact fee study prepared for the City by an independent consultant in 1994[7] to recalculate the fire impact fee schedule by removing the capital facility items in question (i.e., fire apparatus, etc.).

1. Ernst & Young determined the City of Olympia's fire protection facilities inventory as of June 1992 and the 1992 square feet of development served by the current inventory. This was done by removing the capital facilities (i.e., fire apparatus) in question, as seen in Exhibit 14 below.

Exhibit 14 – Fire Apparatus per Square Foot of Development[7]

Component	Number of Apparatuses	Square Feet of Development Served	Apparatus Per Square Foot
Stations	3	38,171,851	.000000078
~~Pumpers~~	~~6~~	~~38,171,851~~	~~.000000157~~
~~Rescue Units~~	~~3~~	~~38,171,851~~	~~.000000078~~
~~Aerial Units~~	~~1~~	~~38,171,851~~	~~.000000026~~
~~Hazardous Materials Units~~	~~1~~	~~38,171,851~~	~~.000000026~~

2. Next, the 1992 cost per inventory item was determined, as well as a cost per square foot. See Exhibit 15 below.

Exhibit 15 – Capital Cost per Square Foot of Development[7]

Component	Apparatus Per Square Foot	Cost Per Apparatus	Capital Cost Per Square Foot
Stations	.000000078	$ 1,684,000	$ .131352
Total Cost/Sq Ft			*$ 0.131352*

3. Previous years' expenditures for fire protection facilities were then determined. See Exhibit 16 below (same as Exhibit 15 shown above).

Exhibit 16 – Previous Expenditures for Fire Protection Facilities[7]

Year	Expenditures
1985	$ 37,870
1986	285,940
1987	137,530
1988	47,120
1989	47,280
1990	42,460
1991	109,780
1992	28,308
1993	36,410
9-Year Total	*$772,698*

4. An annual average of the nine-year total was calculated ($85,855). Using this number, along with the 1992 square feet of development (38,171,851), an annual average per square foot of development was computed as $0.0022491.
5. Using a discount rate of 7%, the net present value of 27.5 years of future payments (at $0.0022491) will total $0.032157 per square foot.

6. Therefore, the fire impact fee rate is $0.099 per square foot ($0.131352 [from Exhibit 19] minus $0.032157).)

Ernst & Young took the new fire impact fee calculation of $0.099 per square foot of development and recalculated under this scenario what should have been collected in fire impact fees over the audit period. Ernst & Young calculated that $305,470 would have been collected; which is $185,656 less than what the City charged under its current calculation.

Comparison of Scenarios 1 and 2 above to the Actual Fire Impact Fees Collected

Finally, Ernst & Young compared the above two fire impact fee calculations to the actual amount of fire impact fees collected by the City of Olympia during the audit period (2004-2006).

Exhibit 17 – Comparison of Potential Fire Impact Fees Collected During the 2004-2006 Performance Audit Period

Actual Fire Impact Fees Collected by the City of Olympia	Potential Fire Impact Fees Collected Under Scenario 1	Potential Fire Impact Fees Collected Under Scenario 2	Potential Fire Impact Fees Collected Based on Use of Updated CFP
$ 491,036	$ 145,723	$ 305,470	
Potential Overcharge	*$ 345,313*	*$ 185,565*	
Potential Undercharge			*?*

In looking at the above table, the City of Olympia has potentially overcharged for fire impact fees anywhere from $185,565 to $345,313; however, please note the potential for an undercharge, as stated below in the final comments to this audit area.

Lastly, Ernst & Young noted that the City of Olympia's fire impact fee schedule/calculation has been the same since its inception in 1994; however, since Ernst & Young only had fire impact fee collection data for the audit period, it was unable to calculate an overcharge for the life of the fire impact fee (i.e., 1994 - 2008).

Please note that this is simply an estimated fire impact fee schedule for the City of Olympia, as growth and historical fire and aid call data was not sufficient from the City. The City asserts it has undercharged the fire impact fee. Ernst and Young believes this assertion may be possible based on the fire impact fee calculation the City uses not being tied to its Capital Facilities Plan (CFP) and the City's CFP appears to not be up-to-date. The City is planning on building a new fire station that costs roughly $7.9 million; however, this facility was not included on the 2003

CFP. Had the City tied its impact fee calculation to its CFP and updated its CFP, it is possible that the City may have undercharged, rather than overcharged. Although, the City provided Ernst & Young population statistics, fire and aid call data, and construction data, it was insufficient to validate the City's assertion.

AUDIT AREA 7 – SCHOOL IMPACT FEE SCHEDULE/CALCULATION

FINDING

Among the Cities that collect school impact fees, there are inconsistencies in determining the level of review of the school impact fee calculation prepared by the school districts.

BACKGROUND

Original Finding Identification

During Phase 1 of the performance audit, Ernst & Young noted that Washington State is unique in that it allows for the assessment of school impact fees. However, school districts in the State of Washington do not have the authority to impose school impact fees. Rather, a district must have impact fees imposed by the city (or cities) and county it resides in. The cities or counties then remit the impact fees collected to the school district through an interlocal agreement. In order for a city to collect fees on behalf of a district, the city must adopt the school district's capital facilities plan (CFP) and its school impact fee schedule.

The Cities develop their own ordinances stating the required reviews of the school district CFP in order for the city to adopt the plan. For example, Ernst & Young noted that in Vancouver, the "Planning Commission" is required to determine a) whether the district's forecasting system for enrollment projections appears reasonable and reliable, b) whether the anticipated level of state and voter-approved funding appears reasonable and historically reliable, and c) whether the district appropriately applied the given formula.

Ernst & Young met with several cities collecting school impact fees in the performance audit period: Maple Valley, Federal Way, Olympia and Vancouver. In initial meetings and communications with these Cities, Ernst & Young determined the Cities may not perform a detailed review of a district's CFP or impact fee calculations, as the Cities emphasized the fee as a "pass-through."

Audit Work Conducted

During Phase 3 of the performance audit, Ernst & Young met with the cities of Olympia and Vancouver to further discuss the review of the school impact fee calculation and schedule.

<u>Fee Calculation and Review in Vancouver</u>

Upon further review, Ernst & Young noted that the calculation of a school district's impact fee schedule is complex and focused on fee accuracy for a specific school district rather than consistency between districts. School impact fees can vary significantly due to the number of independent variables involved in the calculation as well as policy decisions by each school district.

Through additional research and interviews with the City of Vancouver, it was noted that school impact fees undergo a great deal of review, although the review is not entirely at the city level. In general, school impact fees are reviewed by planning staff at the school districts, the Vancouver City Planning Commission, and the Vancouver City Council. Also, the school impact fees undergo public hearings before the school boards.

Before the City of Vancouver reviews the school districts' capital facilities plans, they are first prepared and reviewed by school district planners. They then go through a public hearing process before the school boards approve the school impact fees and the school districts' capital facilities plans. At this point, the school impact fee schedule is submitted to the City for review.

Once with the City, the school districts' capital facilities plans and impact fee schedules are reviewed by the Community Planning department. Community Planning's review includes reviewing the assumptions and reasonableness related to population growth and estimates for development patterns.

After Community Planning review, a staff report is issued to the City Planning Commission. The planning commission holds a public hearing and asks detailed questions about the fees and the source data used to develop the fees as well as the capital facilities plan. Questions are answered by both Community Planning and representatives from each school district who attend the public hearing. After this meeting, the Planning Commission recommendation is forwarded to the City Council, which holds a first reading of the proposed ordinance adopting the district's capital facilities plan and imposing the fee. The City Council subsequently holds a public hearing at which the ordinance is adopted.

Fee Calculation and Review in Olympia

Through further discussions with the City of Olympia, Ernst & Young noted that Olympia is comfortable with the degree of school district review that is performed. Olympia's city-level review of school impact fees takes a lighter approach than the City of Vancouver on a yearly basis, as the underlying calculation has not changed from its in inception in 1994, when the City performed a more detailed review of the approach. Overall, the City of Olympia stated that the City's Planning Committee does not believe it has the capacity to question the school district's capital facilities plan or impact fee calculation, as it does not have the same knowledge of the variables contained in the school impact fee calculation as the school district.

The City of Olympia also stated that the school district's capital facilities plan and impact fee calculation is developed through planners within the school district, and then passes many reviews, including an opportunity for the public to comment, as well as the final acceptance by the school board. The City believes the school district is highly capable, demonstrating a great deal of care in developing its capital facilities plan and impact fee calculation, and therefore Olympia does not feel it needs to perform a detailed review of the school impact fee calculation, its underlying factors, or the capital facilities plan on a yearly basis.

Lack of Specific Review Requirements in RCWs

Washington State law is not specific in providing guidance to cities for adopting school capital facilities plans and impact fees. For this reason, different cities impose different levels of review according to their comfort level with the school district's analysis. While it may seem natural to rely heavily on school district expertise, there may be room for a county's or City's additional review. For example, in September of 2002, a developer sued both a school district and King County over the calculation of school impact fees *(Wellington River Hollow LLC v King County*[5]*).*

RECOMMENDATIONS

The Cities should revisit their review process of the school impact fee calculation/schedule and capital facilities plan, knowing that they may be involved if litigation results from a school impact fee assessed. The Cities should pay particular attention to the City of Vancouver's school impact fee review process, as it has the most in-depth and comprehensive review process.

Note: The cities of Redmond, Maple Valley, and Federal Way also collect school impact fees; however, no detailed performance audit work was conducted at these other Cities. The *performance audit of this area focused on the cities of Olympia and Vancouver, as they exhibited the greatest opportunity during the Phase 1 planning process. The cities of Redmond, Maple Valley, and Federal Way should consider the above recommendations as well.*

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There is no immediate potential cost savings associated with these recommendations. If the cities or Washington State implement these recommendations, Ernst & Young sees the Cities benefitting by having more confidence that the school impact fee they charge is appropriate.

AUDIT AREA 8 – TRANSPORTATION IMPACT FEE SCHEDULE/CALCULATION

FINDING

Redmond employs several leading practices with respect to calculating, charging, and maintaining its transportation impact fee.

BACKGROUND

Original Finding Identification

During Phase 1 of the performance audit, Ernst & Young noted that Maple Valley and Vancouver base their transportation impact fees on the number of trips generated by each development and adopt a per-trip rate (any trip for Vancouver; PM Peak Trips[8] in Maple Valley), and apply those to the number of trips expected to be generated by the development based on the Institute of Traffic Engineers "Trip Generation" manual (ITE manual) or based on an independent traffic engineer's estimate.

We noted that in Redmond and Olympia, transportation impact fees can easily be calculated by the developer, allowing for a reasonable estimate of the costs of the development before the developer sought a building permit, referenced the ITE manual, or obtained an independent traffic study.

Audit Work Conducted

Ernst & Young selected Redmond and Maple Valley for further investigation into the methodology behind their transportation impact fees. Ernst & Young met with representatives from Transportation and Finance and walked through the development of the fee schedule by land use or rate per trip in the City ordinance. Ernst & Young reviewed documentation regarding the fee calculation and discussed ways to enhance the transportation impact fee calculation function.

Both the City of Redmond and the City of Maple Valley assess impact fees that are fundamentally based on a cost-per-growth-trip multiplied by the number of trips expected from the development. In Redmond, the cost element is based on the new costs due to growth in a 20-year Transportation Facilities Plan (TFP). In Maple Valley, the cost element is based on the growth-related costs in the upcoming 6-year component of a 20-year plan, its Transportation

Improvement Program (TIP). In both cities, the number of trips is drawn from a reference manual titled "Trip Generation" published by the Institute of Traffic Engineers (the ITE manual).

Ernst & Young noted several leading practices in Redmond:

<u>Inflation Indexing</u>

The cost element of the impact fee calculation is revised as needed based on how well the TFP reflects actual projected upcoming costs, but also includes an allowance for an administrative adjustment for inflation based on the Washington State Department of Transportation Highway Construction Cost Index. This allows an administrative adjustment to keep the fees and the cost of the impact of new development aligned. To achieve the same goal, Maple Valley goes through an annual City council update of the Six-Year Transportation Improvement Program (TIP) and adoption of an updated fee.

<u>Costs Based on a Long-Range Plan</u>

The City of Redmond noted that a 20-year TFP helps it to be more competitive in seeking out grant funding from other agencies. The City of Maple Valley has also developed a 20-year TFP and has not experienced difficulties in securing grant funding for transportation projects if they are a part of the 6-year TFP. If a project is not in the 6-year TFP and receives grant dollars, the City of Maple Valley will include the project in the 6-year TFP as part of the annual update (discussed above).

However, the City of Redmond noted that in a 6-year plan, the addition of large initiatives, necessary for continued growth, may cause a sudden jump in the transportation impact fee. This impact can be reduced by including more projects in a 20-year plan, thereby leveling out the variability caused by larger projects in the plan.

<u>Adopted Fee Schedules</u>

Once the City of Redmond has established a cost per trip, it further multiplies that cost by the number of trips generated by 39 typical land use categories and adopts a fee schedule into the municipal code (the Redmond Community Development Guide) for each land use based on an appropriate unit of development. Maple Valley noted that this practice may appear to provide better service to the development community by allowing developers to easily estimate their own transportation impact fee before applying for a building permit.

Maple Valley instead adopts a cost per trip based on assessing the most appropriate number of PM peak hour trips based on the transportation administrator's judgment and the ITE manual. Redmond noted no developer inquiries into the basis for its fees, whereas Maple Valley receives inquiries from developers on the number of PM peak hour trips assessed to its developments from time to time. Initially, Ernst & Young had thought that the resources used to analyze each transportation facility could be significantly reduced by the Redmond approach. However, Ernst & Young determined that analysis must still occur for each transportation facility to allow for concurrency, a requirement of other Washington State legislation.

Ernst & Young noted that in Maple Valley, the transportation administrator carefully selects the appropriate land use type (and therefore the number of trips) on a case-by-case basis for each new development from the ITE manual. This level of involvement is not required in Redmond when development falls into one of the 39 pre-defined land-use categories, but an administrative review is allowed when a development may not fit well into the adopted land-use categories. This may result in less staff time necessary in Redmond to process a building permit.

RECOMMENDATIONS

1. Cities should consider implementing a construction cost adjustment to keep transportation impact fees in line with the cost of projects they fund.
2. Cities calculating impact fees based on a short-term project list should consider expanding that list to include projects farther in the future that will be needed due to growth.
3. Cities should adopt a transportation impact fee schedule in their ordinances that allows a developer to easily determine the impact fee to be paid upon building permit issuance. The transportation fee schedule should be based on typical land uses and trips per land use.

Note: The cities of Olympia and Vancouver also collect transportation impact fees; however, no detailed performance audit work was conducted at these other cities. The performance audit of this area focused on the cities of Redmond and Maple Valley, as they exhibited the greatest opportunity. The cities of Olympia and Vancouver should consider the above recommendations as well.

POTENTIAL COST SAVINGS AND OTHER IMPACTS

There is no immediate potential cost savings associated with these recommendations. If Cities implement these recommendations, Ernst & Young sees these benefits:

1. Fees will more closely match the costs they support. This will prevent sudden increases in fees and allow less frequent fee updates.
2. Cities may find that they will charge a less volatile impact fee that better represents the cost of growth.
3. Developers will be able to calculate and understand their transportation impact fees without outside assistance. Cities may also save time in assessing the fee as well.

AUDIT AREA 9 – PERMIT SYSTEM

FINDINGS

1. Redmond records collections, interest earnings, and expenditures of each impact fee received and tracks them in an Access database. The same general information is available in the City's cash receipt system, thus creating a duplication of efforts by entering the impact fee information twice.
2. The cities of Vancouver and Olympia have integrated their permitting systems with their accounting systems. This was identified as a leading practice among the Cities due to the tighter internal controls and lack of manual manipulation.

BACKGROUND

Original Finding Identification

In Phase 1 of the performance audit, Ernst & Young noted varied approaches in tracking the impact fees associated with permits issued. Vancouver uses an IT system called Tidemark Advantage within the Development Review Services department. It provides calculation and tracking of impact fees received. Redmond tracks in detail the collection, expenditure, and interest earnings of individual fees received from developers in a separate Access database created for this purpose.

Audit Work Conducted

During Phase 3 of the performance audit, Ernst & Young researched these varying systems further. First, Ernst & Young gained a detailed understanding of how the City of Vancouver's permit system interfaces with its accounting system. Next, Ernst & Young visited the cities of Olympia and Redmond to gain an understanding of the way their permit systems interfaced with their accounting systems. Ernst & Young did not review Maple Valley's or Federal Way's permit systems, as both cities collect a significantly smaller amount of impact fees.

<u>City of Vancouver's Permit System</u>

The information system used by the City of Vancouver for permit issuance is called Tidemark Advantage (Tidemark). Tidemark is also integrated with the City's accounting system. Tidemark contains a Cashier module, which allows cashiers to receive impact fee receipts against the original documentation and associate all cash receipts with building permits.

Ernst & Young noted that the process of issuing a building permit and collecting the impact fee within Tidemark is as follows:

1. A customer comes to the permit office to pay the impact fees due and obtain a building permit.
2. A permit technician (one who works at the City and issues permits) logs into Tidemark to pull up the building permit application for the customer.
3. The permit technician enters the building permit data. The impact fee data is automatically calculated in the system based on the type of land use (i.e., multi-family, single-family, retail, etc.), the building site address, and the square footage (if necessary). Manual entry (i.e., override) of the impact fee is possible, but not generally utilized, except for single-family transportation impact fees. Ernst & Young noted that there is no review or approval of the overrides.
4. Once all building permit data is entered, an impact fee amount is automatically calculated in Tidemark.
5. The customer then pays a cashier the amount of impact fees owed.
6. The cashier receives the monies paid against the amount owed in Tidemark, and the building permit is issued.

Ernst & Young noted that Tidemark is fully integrated with the City's GL system, Oracle. Each day the Vancouver Accounting Department logs into Oracle and pulls the report generated by Tidemark for the previous day. The report is uploaded into Oracle. The Accounting Department performs a reconciliation of the data between Oracle and Tidemark to determine that all information transferred correctly.

<u>City of Olympia's Permit System</u>

Ernst & Young met with the City of Olympia to gain an understanding of how its permit system works with its accounting system. Olympia tracks impact fees through a permit module of its citywide accounting system, SunGard HTE.

School and park impact fees are coded into the permit module so the fee amounts are calculated by the system. Fire impact fees are automatically calculated by the system once the square footage of the development is entered. Transportation impact fees require a manual entry and are not automatically calculated by the system.

The permitting function is a module of the overall SunGard information system, which also encompasses the City's general ledger and the cashier functions. As a result, there is a daily import function from the permitting module to the general ledger module, which posts impact fee receipts into the corresponding impact fee accounts coded into the system.

City of Redmond's Permit System

In the City of Redmond, staff within the Planning Department complete an *Impact Fee Calculation Form* detailing impact fees and any credits associated with the impact fee. The *Impact Fee Calculation Form* is then provided to the Permits Center. The Permits Center enters the information contained on the *Impact Fee Calculation Form* in the City's permit system, Permits Plus, when a building permit is issued. The fee is not automatically calculated by Permits Plus.

When customers pay for and pick up their building permits, they pay the permitting cashiers. These cashiers work in the cashier module of Permits Plus, which does not integrate with the cashier module of the City's general ledger system. At the end of each day, permit technicians balance their receipts and spend 10-15 minutes per day reconciling the data into Quadrant, the citywide cash receipts software. Quadrant then interfaces daily with E-1, the City's general ledger software, to upload the fees and cash receipts.

In addition, on a monthly basis, the Finance Department enters new impact fees received and allocates interest to each individual impact fee not spent in an Access database. For each impact fee received, an entry is made in the database recording the source, the date, the amount, and the type. Each time a transfer is made out of an impact fee account, the spender e-mails Finance with the project and the amount, and Finance records impact fees as spent and stops allocating interest to them on a first-in-first-out basis. The entry of the impact fee data into the database takes one City employee roughly one full working day each month to complete.

Ernst & Young noted that the information was entered into an Access database starting some time in the early 2000's. This process started due to a request of information from the State Auditor's Office. The State Auditor's Office did not recommend the implementation of the Access database, but rather requested to see which development each impact fee was expended for. The City of Redmond felt that it could best track and provide this information using the Access database. However, Ernst & Young noted that the same information entered into the Access database can be retrieved from Quadrant (the City's cash receipt system), except for the allocation of interest earned to each impact fee. However, in the event that a refund of an impact fee is necessary, any interest allocation can easily be re-calculated. The additional tracking mechanism provided by the Access database is a duplication of efforts in the Accounting Department, as the information is available from the cash receipt system.

RECOMMENDATIONS

1. Redmond should eliminate the Access database tracking of individual impact fee collection, expenditures, and interest allocation to save staff time. This entry is a duplication of efforts, as all data entered into the database is available within Quadrant. The following two items are not available within Quadrant; however, they are not necessary to have, as the information can be regenerated, if needed:
    a. Interest Allocation: Currently, the City of Redmond is allocating interest earned to each individual impact fee. Because the City of Redmond utilizes only one zone for each type of impact fee, this is unnecessary, as fees collected within the City can be spent anywhere in the City. The interest can simply be allocated to the impact fee GL account for each type of fee and can therefore be spent on a first-in, first-out basis, along with the impact fees.
    b. Impact Fee Spending: Currently, the City of Redmond ties each impact fee to the project it was spent on. The tracking to this degree is extremely time-consuming and unnecessary. Because the City of Redmond utilizes one zone for each type of impact fee, this is unnecessary, as fees collected within the City can be spent anywhere in the City. The fees are spent on a first-in, first-out basis, and therefore there is no need to continue tracking with the Access database.
2. All Cites (Vancouver, Redmond, Federal Way, Maple Valley, and Olympia) should maintain a permit system that automatically interfaces with the city accounting system. A leading practice would be the systems of Vancouver and Olympia. In addition to the automatic interface, the following functions or reviews should be conducted to tighten internal controls:
    a. All impact fees should be automatically calculated by the system, with the understanding that there will always be times when a fee needs to be manually overridden.
    b. Fees that are manually overridden should be reviewed on a periodic basis to determine that the overrides are valid and accurate.

c. Access to the permitting system should be restricted to only those city employees who demonstrate the need for access.
d. Access to the cash receipts module should be restricted to only those city employees who demonstrate the need for access.

POTENTIAL COST SAVINGS AND OTHER IMPACTS

Recommendation 1

To develop a potential cost savings for recommendation 1 above, Ernst & Young calculated the amount of time spent by the City of Redmond entering impact fee data into the Access database. Ernst & Young noted that there is one individual who enters impact fee information into the Access database each month. In addition, there are three individuals who prepare expenditure information on an annual basis for fire, park, and transportation impact fees. This information is then sent to the individual who enters the expenditures into the database. Once Ernst & Young determined the amount of time spent on the tasks, Ernst & Young obtained Redmond employee salary data and information from the Bureau of Labor Statistics about the total cost of employment and annual increases in compensation costs for public-sector employees. A ten-year potential cost savings (2004–2013) was then determined for elimination of the task. See Exhibits 18 and 19 below for calculation information.

Exhibit 18 – Potential Cost Savings for the Elimination of Access Database – Data Entry

Employee estimate of hours task requires monthly	6 Hours
Hourly employee cost – City of Redmond Accountant (2003)	$ 37.66
Annual cost of the task (hours x salary)	$ 2,711.52
Historical average annual increase in compensation costs	3.88%
2004 cost	$ 2,816.73
Potential 10-year cost savings	**$ 33,638.78**

Exhibit 19 – Potential Cost Savings for the Elimination of Access Database – Expenditure Preparation

Employee estimate of hours task requires yearly	48 Hours
Hourly employee cost – City of Redmond Accountant (2003)	$ 31.88
Annual cost of the task (hours x salary)	$ 1,530.24
Historical average annual increase in compensation costs	3.88%
2004 cost	$ 1,589.61
Potential 10-year cost savings	**$ 18,951.79**

Recommendation 2

There appears to be only one task across the three Cities reviewed that, if eliminated, would save time and money – the reconciliation of cash receipt data from Permits Plus to Quadrant by the City of Redmond. Ernst & Young determined the amount of time spent on the task and then obtained Redmond employee salary data and information from the Bureau of Labor Statistics about the total cost of employment and annual increases in compensation costs for public-sector employees. A ten-year potential cost savings (2004–2013) was then determined for elimination of the task. See Exhibit 20 below for calculation information.

Exhibit 20 – Potential Cost Savings for the Elimination of the Cash Receipts Reconciliation Performed by the City of Redmond

Employee estimate of hours task requires daily	0.25
Hourly employee cost – City of Redmond Permit Technician	$ 31.83
Estimated daily cost	$ 7.96
Estimated annual cost	$ 1,909.81
Historical average annual increase in compensation costs	3.88%
2004 cost	$ 1,983.91
Estimated 10-year cost	**$ 23,689.74**

Ernst & Young recognizes that implementation of the above recommendation will require resources; however, this performance audit did not look into the costs of implementing the above recommendation.

Potential 10-Year cost savings from implementing both recommendations: $76,280.31

END NOTES

[1] MRSC: Municipal Research and Services Center (MRSC) is a nonprofit organization that provides guidance to local governments on issues of legal concern.

[2] City of Olympia's 1999 Capital Facilities Plan: http://www.olympiawa.gov/citygovernment/budget

[3] Olympia's Park and Open Space Standards and Definitions document: http://www.ci.olympia.wa.us/cityservices/par/parplan/

[4] Resident Opinions of City Government Services Survey (City of Olympia – December 2006): http://www.ci.olympia.wa.us/NR/rdonlyres/8A5A307E-012E-467E-B594-8B7AC842F677/0/CCS_Report_2006.pdf

[5] Wellington River Hollow LLC v King County: http://caselaw.lp.findlaw.com/scripts/getcase.pl?court=wa&vol=2002_app/47976-8&invol=3

[6] City of Olympia's 2007 Capital Facilities Plan: http://www.olympiawa.gov/citygovernment/budget
[7] *City of Olympia, Impact Fee Rate Study for Fire Protection Facilities.* November 30, 1994.
The Impact Fee Rate Study was prepared by an independent consultant and was adopted by Olympia ordinance 5490. Ernst & Young obtained the rate study from the City of Olympia planning department.

[8] PM Peak Trip: A "PM Peak Trip" is a transportation trip during peak hours in the afternoon.

[9] City of Olympia's 2004 Capital Facilities Plan:

APPENDIX A
I-900 Elements

Appendix A provides a chart showing each I-900 element and where each is addressed in the performance audit findings.

	I-900 Element	Audit Area 1	Audit Area 2	Audit Area 3	Audit Area 4	Audit Area 5	Audit Area 6	Audit Area 7	Audit Area 8	Audit Area 9
1	Identification of potential cost savings (or other financial impact)	●		●		●	●			●
2	Identification of services the can be reduced or eliminated								●	●
3	Identification of programs or services that can be transferred to the private sector. *Because governments must use impact fees for purposes of addressing new development and must do so in a manner that complies with state laws, Ernst & Young does not believe that these responsibilities should be transferred to the private sector.*									
4	Analysis of gaps or overlaps in programs or services and recommendations to correct gaps or overlays	●	●		●	●		●		
5	Feasibility of pooling the entity's information technology systems									●
6	Analysis of roles and functions of the entity and recommendations to change or eliminate roles or functions							●		●
7	Recommendations for statutory or regulatory changes that may be necessary for the entity to properly carry out its functions	●		●	●		●	●	●	
8	Analysis of the entity's performance data, performance measures, and self-assessment systems[1]						●			
9	Identification of best practices		●	●	●	●	●	●	●	●

Note[1]: Audit Area 6 - The City of Olympia's fire impact fee calculation is not based on a current capital facilities plan that details improvements which are necessitated by new development. Therefore, the City has difficultly in showing that it is charging the correct amount for fire impact fee and spending them on capital facilities that benefit new development.

APPENDIX B
Recommendations Requiring Legislative Action

We recommend the Washington Legislature.

- Amend RCW 82.02.090 to better define capital facilities and alleviate ambiguity.

- Consider modifying RCW 82.02.070 to better define "separate interest-bearing accounts."

APPENDIX C
Recommendations Requiring Changes to City Policy

Appendix C contains a list of the recommendations provided in this report that require changes to city policy.

- The City of Olympia should consider dividing the city into two park zones to demonstrate a clear relationship between where impact fees are collected and spent. At least two zones for park impact fees would appear to be reasonable, given the city's six (6) mile expanse.

- The City of Olympia should consider removing the "one-half to one mile" and "10–20 minute walk" from its definition of a "Neighborhood Park."

- The City of Olympia should revisit its fire impact fee schedule. Specifically, Olympia should more effectively address RCW 82.02.050 and 82.02.060 in its calculation and provide support that the fire impact fee charged relates to system improvements that are reasonably attributable to growth.

- Cities should consider implementing a construction cost adjustment to keep transportation impact fees in line with the cost of projects they fund.

- Cities should adopt a transportation impact fee schedule in their ordinances that allows a developer to easily determine the impact fee to be paid upon building permit issuance. The transportation fee schedule should be based on typical land uses and trips per land use.

Other Observations Outside of the Scope of the Audit to Consider

To improve citizen access to public information, we recommend cities publish their annual impact fee reports online. Currently, cities that collect impact fees are required to prepare an annual impact fee report per RCW 82.02.070:

"Annually, each county, city, or town imposing impact fees shall provide a report on each impact fee account showing the source and amount of all moneys collected, earned, or received and system improvements that were financed in whole or in part by impact fees."

It was noted that cities are preparing these annual reports; however the information is generally not published or available online. Requiring the cities to publish these annual reports online would help to facilitate the State of Washington's initiative to increase transparency and accountability of government agencies and programs.

APPENDIX D
Summary of Leading Practices by City

Appendix D provides a chart showing the leading practices identified throughout the report and which city the leading practices were identified in.

	LEADING PRACTICE	CITY				
		Redmond	Federal Way	Maple Valley	Olympia	Vancouver
1	The City of Redmond Fire Department has developed a leading practice in its relationship with Fire District 34. Specifically, the City of Redmond Fire Department's method to allocate costs of new capital facilities between the city and Fire District 34 should be evaluated for implementation in other Cities and districts.	✓				
2	The City of Vancouver uses the Emphasys SymPro system (SymPro) to assist in managing the city treasury function, including the interest allocation. SymPro tracks investment earnings and interfaces with the city's general ledger to retrieve the daily balances for all accounts to which to allocate interest. Investment earnings are then allocated across the general ledger accounts based on their average daily balances.					✓

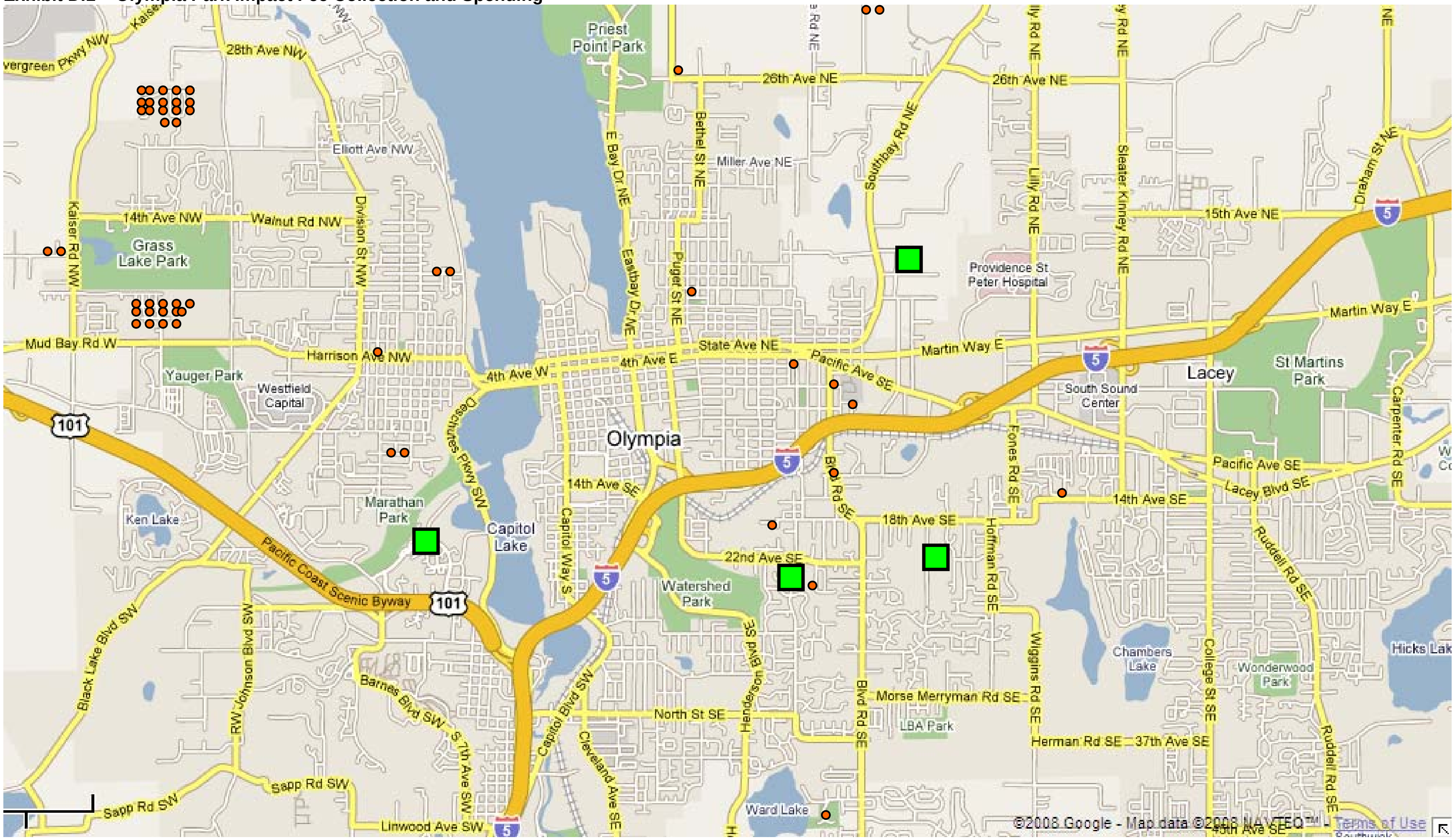
	LEADING PRACTICE	CITY				
		Redmond	Federal Way	Maple Valley	Olympia	Vancouver
3	Ernst & Young noted that the City of Redmond's fire impact fee calculation and schedule met all aspects of RCW 82.02.050 and 82.02.060 and demonstrates a leading practice. Redmond's fire impact fee calculation and schedule takes the following items into consideration: • System improvements that are reasonably related to growth • The proportionate share of the costs of system improvements related to new development	✓				
4	The City of Vancouver's school impact fee review process is a leading practice, as the City demonstrates the most in-depth and comprehensive review of the school impact fee calculation and schedule.					✓
5	Redmond employs several leading practices with respect to calculating, charging, and maintaining its transportation impact fee. These leading practices include: • Inflation indexing • Costs based on a long-range plan • Adopted fee schedules by land-use	✓		✓[1]		✓[1]
6	The cities of Vancouver and Olympia have integrated their permitting systems with their accounting systems. This was identified as a leading practice among the Cities due to the tighter internal controls and lack of manual manipulation.				✓	✓

[1] The cities of Maple Valley and Vancouver both use inflation indexing.

APPENDIX E
Olympia Park Impact Fee Collection and Spending

Ernst & Young conducted an analysis of park impact fee collections and expenditures in the City of Olympia for the performance audit period (2004–2006). Ernst & Young randomly selected a sample of 50 park impact fees collected during the audit period and found that the average distance between the location where an impact fee was collected and the location where the impact fee was potentially used on a neighborhood park was approximately four and one-half miles. Appendix D provides a detailed map showing the sample of 50 park impact fees collected (red circles), as well as where the park impact fees were potentially spent (green squares). Refer to Section 6*, Audit Area 3 – Park Zoning,* for more details surrounding the sample of 50 park impact fees.

Exhibit D.1 – Olympia Park Impact Fee Collection and Spending



Location of Where Impact Fee Was Collected

Location of Neighborhood Park Where Impact Fee Was Potentially Spent

APPENDIX F
Elements of Findings

According to Government Auditing Standards (GAS), "To the extent possible, in presenting audit findings such as deficiencies in internal control auditors should develop the elements of criteria, condition, cause and effect to assist management or oversight officials of the audited entity in understanding the need for taking corrective action. In addition, if auditors are able to sufficiently develop the findings, they should provide recommendations for corrective action."

E&Y has included all the elements discussed above; however, they are not specifically called out in the report. Therefore, a summary for each area and finding was created to show the condition, cause, criteria, effect, and recommendation.

The table below defines what each element of a finding is, according to GAS:

Element of Finding	Description
Condition	Identifies the nature of the deficiency, finding, or unsatisfactory condition by disclosing how things are.
Criteria	Establishes the legitimacy of the finding disclosing how things should be.
Cause	Gets to the root of the problem by answering the question, "Why did it happen?"
Effect	Convinces the reader that the condition is significant by answering the question, "What happened as a result of this condition? How was the government or taxpayer harmed?"
Recommendation	Suggests remedial action. If the relationship between the cause and the condition is clear and logical, the recommended action will most likely be feasible and appropriately directed.

Finding	Element of Finding: Condition	Element of Finding: Criteria	Element of Finding: Cause	Element of Finding: Effect	Recommendation
RCW 82.02.090 defines the term capital facilities for fire, transportation, park, and school impact fees. However, the definitions provided are ambiguous, resulting in Cities applying varying interpretations of the definition of a “capital facility.”	Cities are unclear as to what types of expenditures are appropriate for impact fees.	Cities ought to be consistent in applying the definition of a capital facility where impact fees are used as a funding source.	It is unclear in Washington State law if the term "capital facilities" includes fire rescue equipment, sidewalks, school buses, etc.	Cities are questioned by the public as to the validity of capital purchases.	Ernst & Young recommends that Washington State amend RCW 82.02.090 to better define capital facilities and alleviate the ambiguity.
The City of Redmond Fire Department has developed a leading practice in its relationship with King County Fire District No. 34. Specifically, the City of Redmond Fire Department’s method to allocate costs of new capital facilities between the city and Fire District No. 34 should be evaluated for implementation in other cities and districts.	Impact fees are spent on facilities used by both a fire department and a fire district.	Impact fees should be expended for facilities used by a fire department.	Some Cities have shared facilities between the fire district and fire department.	Redmond benefits from shared facilities, while maintaining separate funding sources through the use of an allocation tool.	Other cities within the State of Washington should be aware of this leading practice and attempt to implement a similar contract if the city has a relationship with a neighboring fire district.
The use of multiple zones is seen as an effective way to reasonably relate the collection and expenditures of park	Neighborhood parks are funded by impact fees collected outside of their service areas.	Olympia should fund neighborhood parks with impact fees collected from developments according to the city's	Olympia's neighborhood park system is designed to serve the whole community of Olympia, with	Neighborhood park development appears to not relate to growth.	Consider removing the “one-half to one mile” and “10–20 minute walk” from its definition of a “Neighborhood Park.”

Finding	Element of Finding: Condition	Element of Finding: Criteria	Element of Finding: Cause	Element of Finding: Effect	Recommendation
impact fees to areas experiencing growth. Based on the use of one zone, the City of Olympia is potentially spending neighborhood park impact fees that are inconsistent with its definition of a neighborhood park and results of a citizen survey. Therefore, the City of Olympia may not be spending park impact fees as effectively as it could using multiple zones. .		service definition.	eventual goals of serving citizens within a one-half to one mile of the park.		And Consider dividing the City into two park zones to demonstrate a clear relationship between where impact fees are collected and spent. At least two zones for park impact fees would appear to be reasonable, given the City's six (6) mile expanse.
Interest allocation methods used by each City to allocate interest to impact fee general ledger (GL) accounts vary among the Cities. The City of Vancouver's interest allocation method is a leading practice among the Cities.	The City of Vancouver's interest allocation method is a leading practice among the Cities.	Other Cities allocate interest in manual processes involving off-system accounts tracked in spreadsheets.	The requirement in the RCW that impact fees be maintained in separate interest-bearing accounts is interpreted differently by various individuals.	Implementing treasury software such as Vancouver's may improve efficiency and accountability	The Cities should consider procuring a treasury management system similar to that of the City of Vancouver, which allows for a daily allocation of interest and minimal manual involvement. Cities should allocate interest based on actual interest earned, rather than allocating interest using a rate that is near but not equal to

Finding	Element of Finding: Condition	Element of Finding: Criteria	Element of Finding: Cause	Element of Finding: Effect	Recommendation
					the actual interest earned. Washington State should consider modifying RCW 82.02.070 to better define “separate interest-bearing accounts.”
The cities of Olympia and Federal Way do not remit any interest earned on school impact fees they receive to the school districts; therefore, the interest earned while the impact fees were invested does not appear to be expended for the purpose for which the impact fee was imposed, as required by RCW 82.02.070.	The cities of Olympia and Federal Way earn interest on school impact fees before they are remitted to the school district. Interest earnings are not remitted and are therefore not expended for the purpose for which the fee was established.	The cities of Olympia and Federal Way should remit the impact fee as well as the interest earned while acting as custodians.	The original agreements between the school districts and the Cities did not require the city to remit interest.	Interest on impact fee receipts was not expended for the purpose for which the fee was collected. This is in violation of RCW 82.02.070.	The Cities should allocate both past and future actual interest earnings to school impact fees collected and remit those interest earnings to the appropriate school district(s).
The City of Redmond has developed a leading practice in its fire impact fee schedule/calculation, specifically the method it utilizes takes into account the impacts of fire and aid calls by land use type, projected growth by land use type and the	Olympia's fire impact fee rate has not been recently reviewed, and lacks relation to current conditions.	Impact fee calculations/schedules should be up-to-date and in compliance with applicable RCWs.	Olympia was unaware of how the fire impact fee calculation was determined.	Olympia's fire impact fees do not accurately reflect the impact of a development on the city's fire protection facilities.	Other cities within the State of Washington should be aware of the City of Redmond’s leading practice for the fire impact fees schedule/calculation. The City of Olympia should revisit its fire impact fee schedule and consider if it is

Finding	Element of Finding: Condition	Element of Finding: Criteria	Element of Finding: Cause	Element of Finding: Effect	Recommendation
fire Capital Facilities Plan (CFP). The City of Olympia's fire impact fee schedule/calculation does not appear effectively demonstrate the fee's connection to system improvements related to growth, or the cost of public facilities necessitated by new development or the availability of other financing.					suitable to continue charging the fire impact fee. Specifically, Olympia should more effectively address RCW 82.02.050 and 82.02.060 in its calculation and provide support that the fire impact fee charged reasonably relates to system improvements that are reasonably attributable to growth. Additionally, the City of Olympia should consider implementing a periodic review of its fire impact fee calculation and schedule to determine if the fee is still adequate, given its capital facilities plan (i.e., the city's capital facility needs and anticipated growth).
Among the Cities that collect school impact fees, there are inconsistencies in determining the level of review of the school impact fee	Some Cities perform a limited review of school impact fees before adopting them and accepting responsibility.	Those responsible for imposing school impact fees ought to review and understand their calculation.	Cities impose school impact fees that are prepared externally and deal with unfamiliar planning considerations.	Cities are at risk to defend a fee they are not familiar with.	The Cities should revisit their review process of the school impact fee calculation/schedule and capital facilities plan, knowing that

Finding	Element of Finding: Condition	Element of Finding: Criteria	Element of Finding: Cause	Element of Finding: Effect	Recommendation
calculation prepared by the school districts.					they may be involved if litigation results from the school impact fee assessed.
Redmond employs several leading practices with respect to calculating, charging, and maintaining its transportation impact fee.	We consider elements of Redmond's transportation impact fee processes as leading practices among the Cities.	Transportation fee administration should be simple and the fees should be easily identifiable for developers.	Redmond has given significant attention to its transportation impact fee processes.	Other Cities and their citizens may benefit by implementing elements used in Redmond's transportation impact fee process.	Cities should consider implementing a construction cost adjustment to keep transportation impact fees in line with the cost of projects they fund. Cities calculating impact fees based on a short-term project list should consider expanding that list to include projects farther in the future to better compensate for long-term growth. Cities should adopt a transportation impact fee schedule in their ordinances that allows a developer to easily determine the impact fee to be paid upon building permit issuance. The transportation fee schedule should be based on typical land uses and trips per land use.
The cities of	These Cities have	Cities should have	The Cities process a	The systems reduce	All Cities (Vancouver,

Finding	Element of Finding: Condition	Element of Finding: Criteria	Element of Finding: Cause	Element of Finding: Effect	Recommendation
Vancouver and Olympia have integrated their permitting systems with their accounting systems. This was identified as a leading practice among the Cities, resulting in more effective internal controls and limiting manual manipulation.	permit systems that calculate impact fees efficiently and accurately.	permit systems that allow for tight internal controls and minimal manual involvement.	high volume of building permits and impact fees, resulting in implementation of an automated system to enhance efficiency in the process.	the probability of errors and aid in reporting.	Redmond, Federal Way, Maple Valley, and Olympia) should maintain a permit system that automatically interfaces with the city accounting system. Leading practices would be the cities of Vancouver and Olympia's systems.
Redmond records collection, interest earnings, and expenditure of each impact fee received in an Access database. The same general information is available in the city's cash receipt system, creating a duplication of efforts by entering the impact fee information twice.	A duplication of efforts exists in the City of Redmond, in that information is entered into systems twice.	Impact fee data should only be entered into one system.	The city felt that it needed better reporting information; however, this was prior to moving to one zone for all impact fees.	Excess time and money are spent entering data twice.	Redmond should eliminate the Access database tracking of individual impact fee collection, expenditures, and interest allocation to save staff time. This entry is a duplication of efforts, as all data entered into the database is available within the city's cash receipt system.

APPENDIX G
Complete Text of Statutes Referenced Throughout the Report

Appendix G contains the complete text of all statutes referenced throughout the performance audit report. The statute information shown below was taken directly from the Revised Code of Washington (RCW). The Revised Code of Washington is the compilation of all permanent laws currently in force.

RCW 82.02.050
Impact fees – Intent – Limitations.

(1) It is the intent of the legislature:

(a) To ensure that adequate facilities are available to serve new growth and development;

(b) To promote orderly growth and development by establishing standards by which counties, cities, and towns may require, by ordinance, that new growth and development pay a proportionate share of the cost of new facilities needed to serve new growth and development; and

(c) To ensure that impact fees are imposed through established procedures and criteria so that specific developments do not pay arbitrary fees or duplicative fees for the same impact.

(2) Counties, cities, and towns that are required or choose to plan under RCW 36.70A.040 are authorized to impose impact fees on development activity as part of the financing for public facilities, provided that the financing for system improvements to serve new development must provide for a balance between impact fees and other sources of public funds and cannot rely solely on impact fees.

(3) The impact fees:

(a) Shall only be imposed for system improvements that are reasonably related to the new development;

(b) Shall not exceed a proportionate share of the costs of system improvements that are reasonably related to the new development; and

(c) Shall be used for system improvements that will reasonably benefit the new development.

(4) Impact fees may be collected and spent only for the public facilities defined in RCW 82.02.090 which are addressed by a capital facilities plan element of a comprehensive land use plan adopted pursuant to the provisions of RCW 36.70A.070 or the provisions for comprehensive plan adoption contained in chapter 36.70, 35.63, or 35A.63 RCW. After the date a county, city, or town is required to adopt its development regulations under chapter 36.70A RCW, continued authorization to collect and expend impact fees shall be contingent on the county, city, or town adopting or revising a comprehensive plan in compliance with RCW 36.70A.070, and on the capital facilities plan identifying:

(a) Deficiencies in public facilities serving existing development and the means by which existing deficiencies will be eliminated within a reasonable period of time;

(b) Additional demands placed on existing public facilities by new development; and

(c) Additional public facility improvements required to serve new development.

If the capital facilities plan of the county, city, or town is complete other than for the inclusion of those elements which are the responsibility of a special district, the county, city, or town may impose impact fees to address those public facility needs for which the county, city, or town is responsible.

RCW 82.02.060
Impact fees – Local ordinances – Required provisions.

The local ordinance by which impact fees are imposed:

(1) Shall include a schedule of impact fees which shall be adopted for each type of development activity that is subject to impact fees, specifying the amount of the impact fee to be imposed for each type of system improvement. The schedule shall be based upon a formula or other method of calculating such impact fees. In determining proportionate share, the formula or other method of calculating impact fees shall incorporate, among other things, the following:

(a) The cost of public facilities necessitated by new development;

(b) An adjustment to the cost of the public facilities for past or future payments made or reasonably anticipated to be made by new development to pay for particular system improvements in the form of user fees, debt service payments, taxes, or other payments earmarked for or proratable to the particular system improvement;

(c) The availability of other means of funding public facility improvements;

(d) The cost of existing public facilities improvements; and

(e) The methods by which public facilities improvements were financed;

(2) May provide an exemption for low-income housing, and other development activities with broad public purposes, from these impact fees, provided that the impact fees for such development activity shall be paid from public funds other than impact fee accounts;

(3) Shall provide a credit for the value of any dedication of land for, improvement to, or new construction of any system improvements provided by the developer, to facilities that are identified in the capital facilities plan and that are required by the county, city, or town as a condition of approving the development activity;

(4) Shall allow the county, city, or town imposing the impact fees to adjust the standard impact fee at the time the fee is imposed to consider unusual circumstances in specific cases to ensure that impact fees are imposed fairly;

(5) Shall include a provision for calculating the amount of the fee to be imposed on a particular development that permits consideration of studies and data submitted by the

developer to adjust the amount of the fee;

(6) Shall establish one or more reasonable service areas within which it shall calculate and impose impact fees for various land use categories per unit of development;

(7) May provide for the imposition of an impact fee for system improvement costs previously incurred by a county, city, or town to the extent that new growth and development will be served by the previously constructed improvements provided such fee shall not be imposed to make up for any system improvement deficiencies.

RCW 82.02.070
Impact fees – Retained in special accounts – Limitations on use – Administrative appeals.

(1) Impact fee receipts shall be earmarked specifically and retained in special interest-bearing accounts. Separate accounts shall be established for each type of public facility for which impact fees are collected. All interest shall be retained in the account and expended for the purpose or purposes for which the impact fees were imposed. Annually, each county, city, or town imposing impact fees shall provide a report on each impact fee account showing the source and amount of all moneys collected, earned, or received and system improvements that were financed in whole or in part by impact fees.

(2) Impact fees for system improvements shall be expended only in conformance with the capital facilities plan element of the comprehensive plan.

(3) Impact fees shall be expended or encumbered for a permissible use within six years of receipt, unless there exists an extraordinary and compelling reason for fees to be held longer than six years. Such extraordinary or compelling reasons shall be identified in written findings by the governing body of the county, city, or town.

(4) Impact fees may be paid under protest in order to obtain a permit or other approval of development activity.

(5) Each county, city, or town that imposes impact fees shall provide for an administrative appeals process for the appeal of an impact fee; the process may follow the appeal process for the underlying development approval or the county, city, or town may establish a separate appeals process. The impact fee may be modified upon a determination that it is proper to do so based on principles of fairness. The county, city, or town may provide for the resolution of disputes regarding impact fees by arbitration.

RCW 82.02.090
Impact fees – Definitions.

Unless the context clearly requires otherwise, the following definitions shall apply in RCW 82.02.050 through 82.02.090:

(1) "Development activity" means any construction or expansion of a building, structure, or

use, any change in use of a building or structure, or any changes in the use of land, that creates additional demand and need for public facilities.

(2) "Development approval" means any written authorization from a county, city, or town which authorizes the commencement of development activity.

(3) "Impact fee" means a payment of money imposed upon development as a condition of development approval to pay for public facilities needed to serve new growth and development, and that is reasonably related to the new development that creates additional demand and need for public facilities, that is a proportionate share of the cost of the public facilities, and that is used for facilities that reasonably benefit the new development. "Impact fee" does not include a reasonable permit or application fee.

(4) "Owner" means the owner of record of real property, although when real property is being purchased under a real estate contract, the purchaser shall be considered the owner of the real property if the contract is recorded.

(5) "Proportionate share" means that portion of the cost of public facility improvements that are reasonably related to the service demands and needs of new development.

(6) "Project improvements" mean site improvements and facilities that are planned and designed to provide service for a particular development project and that are necessary for the use and convenience of the occupants or users of the project, and are not system improvements. No improvement or facility included in a capital facilities plan approved by the governing body of the county, city, or town shall be considered a project improvement.

(7) "Public facilities" means the following capital facilities owned or operated by government entities: (a) Public streets and roads; (b) publicly owned parks, open space, and recreation facilities; (c) school facilities; and (d) fire protection facilities in jurisdictions that are not part of a fire district.

(8) "Service area" means a geographic area defined by a county, city, town, or intergovernmental agreement in which a defined set of public facilities provide service to development within the area. Service areas shall be designated on the basis of sound planning or engineering principles.

(9) "System improvements" mean public facilities that are included in the capital facilities plan and are designed to provide service to service areas within the community at large, in contrast to project improvements.

RCW 36.70A.070
Comprehensive plans – Mandatory elements.

The comprehensive plan of a county or city that is required or chooses to plan under RCW 36.70A.040 shall consist of a map or maps, and descriptive text covering objectives, principles, and standards used to develop the comprehensive plan. The plan shall be an internally consistent document and all elements shall be consistent with the future land use map. A comprehensive plan shall be adopted and amended with public participation as provided in RCW 36.70A.140.

Each comprehensive plan shall include a plan, scheme, or design for each of the following:

(1) A land use element designating the proposed general distribution and general location and extent of the uses of land, where appropriate, for agriculture, timber production, housing, commerce, industry, recreation, open spaces, general aviation airports, public utilities, public facilities, and other land uses. The land use element shall include population densities, building intensities, and estimates of future population growth. The land use element shall provide for protection of the quality and quantity of groundwater used for public water supplies. Wherever possible, the land use element should consider utilizing urban planning approaches that promote physical activity. Where applicable, the land use element shall review drainage, flooding, and storm water run-off in the area and nearby jurisdictions and provide guidance for corrective actions to mitigate or cleanse those discharges that pollute waters of the state, including Puget Sound or waters entering Puget Sound.

(2) A housing element ensuring the vitality and character of established residential neighborhoods that: (a) Includes an inventory and analysis of existing and projected housing needs that identifies the number of housing units necessary to manage projected growth; (b) includes a statement of goals, policies, objectives, and mandatory provisions for the preservation, improvement, and development of housing, including single-family residences; (c) identifies sufficient land for housing, including, but not limited to, government-assisted housing, housing for low-income families, manufactured housing, multifamily housing, and group homes and foster care facilities; and (d) makes adequate provisions for existing and projected needs of all economic segments of the community.

(3) A capital facilities plan element consisting of: (a) An inventory of existing capital facilities owned by public entities, showing the locations and capacities of the capital facilities; (b) a forecast of the future needs for such capital facilities; (c) the proposed locations and capacities of expanded or new capital facilities; (d) at least a six-year plan that will finance such capital facilities within projected funding capacities and clearly identifies sources of public money for such purposes; and (e) a requirement to reassess the land use element if probable funding falls short of meeting existing needs and to ensure that the land use element, capital facilities plan element, and financing plan within the capital facilities plan element are coordinated and consistent. Park and recreation facilities shall be included in the capital facilities plan element.

(4) A utilities element consisting of the general location, proposed location, and capacity of all existing and proposed utilities, including, but not limited to, electrical lines, telecommunication lines, and natural gas lines.

(5) Rural element. Counties shall include a rural element including lands that are not designated for urban growth, agriculture, forest, or mineral resources. The following provisions shall apply to the rural element:

(a) Growth management act goals and local circumstances. Because circumstances vary from county to county, in establishing patterns of rural densities and uses, a county may consider local circumstances, but shall develop a written record explaining how the rural element harmonizes the planning goals in RCW 36.70A.020 and meets the requirements of this chapter.

(b) Rural development. The rural element shall permit rural development, forestry, and agriculture in rural areas. The rural element shall provide for a variety of rural densities, uses, essential public facilities, and rural governmental services needed to serve the permitted densities and uses. To achieve a variety of rural densities and uses, counties may provide for clustering, density transfer, design guidelines, conservation easements, and other innovative techniques that will accommodate appropriate rural densities and uses that are not characterized by urban growth and that are consistent with rural character.

(c) Measures governing rural development. The rural element shall include measures that apply to rural development and protect the rural character of the area, as established by the county, by:

(i) Containing or otherwise controlling rural development;

(ii) Assuring visual compatibility of rural development with the surrounding rural area;

(iii) Reducing the inappropriate conversion of undeveloped land into sprawling, low-density development in the rural area;

(iv) Protecting critical areas, as provided in RCW 36.70A.060, and surface water and groundwater resources; and

(v) Protecting against conflicts with the use of agricultural, forest, and mineral resource lands designated under RCW 36.70A.170.

(d) Limited areas of more intensive rural development. Subject to the requirements of this subsection and except as otherwise specifically provided in this subsection (5)(d), the rural element may allow for limited areas of more intensive rural development, including necessary public facilities and public services to serve the limited area as follows:

(i) Rural development consisting of the infill, development, or redevelopment of existing commercial, industrial, residential, or mixed-use areas, whether characterized as shoreline development, villages, hamlets, rural activity centers, or crossroads developments.

(A) A commercial, industrial, residential, shoreline, or mixed-use area shall be subject to the requirements of (d)(iv) of this subsection, but shall not be subject to the requirements of (c)(ii) and (iii) of this subsection.

(B) Any development or redevelopment other than an industrial area or an industrial use within a mixed-use area or an industrial area under this subsection (5)(d)(i) must be principally designed to serve the existing and projected rural population.

(C) Any development or redevelopment in terms of building size, scale, use, or intensity shall be consistent with the character of the existing areas. Development and redevelopment may include changes in use from vacant land or a previously existing use so long as the new use conforms to the requirements of this subsection (5);

(ii) The intensification of development on lots containing, or new development of, small-scale recreational or tourist uses, including commercial facilities to serve those recreational or tourist uses, that rely on a rural location and setting, but that do not include new residential development. A small-scale recreation or tourist use is not required to be principally designed to serve the existing and projected rural population. Public services and public facilities shall be limited to those necessary to serve the recreation or tourist use and shall be provided in a manner that does not permit low-density sprawl;

(iii) The intensification of development on lots containing isolated nonresidential uses or new development of isolated cottage industries and isolated small-scale businesses that are not principally designed to serve the existing and projected rural population and nonresidential uses, but do provide job opportunities for rural residents. Rural counties may allow the expansion of small-scale businesses as long as those small-scale businesses conform with the rural character of the area as defined by the local government according to *RCW 36.70A.030(14). Rural counties may also allow new small-scale businesses to utilize a site previously occupied by an existing business as long as the new small-scale business conforms to the rural character of the area as defined by the local government according to *RCW 36.70A.030(14). Public services and public facilities shall be limited to those necessary to serve the isolated nonresidential use and shall be provided in a manner that does not permit low-density sprawl;

(iv) A county shall adopt measures to minimize and contain the existing areas or uses of more intensive rural development, as appropriate, authorized under this subsection. Lands included in such existing areas or uses shall not extend beyond the logical outer boundary of the existing area or use, thereby allowing a new pattern of low-density sprawl. Existing areas are those that are clearly identifiable and contained and where there is a logical boundary delineated predominately by the built environment, but that may also include undeveloped lands if limited as provided in this subsection. The county shall establish the logical outer boundary of an area of more intensive rural development. In establishing the logical outer boundary the county shall address (A) the need to preserve the character of existing natural neighborhoods and communities, (B) physical boundaries such as bodies of water, streets and highways, and land forms and contours, (C) the prevention of abnormally irregular boundaries, and (D) the ability to provide public facilities and public services in a manner that does not permit low-density sprawl;

(v) For purposes of (d) of this subsection, an existing area or existing use is one that was in existence:

(A) On July 1, 1990, in a county that was initially required to plan under all of the provisions of this chapter;

(B) On the date the county adopted a resolution under RCW 36.70A.040(2), in a county that is planning under all of the provisions of this chapter under RCW 36.70A.040(2); or

(C) On the date the office of financial management certifies the county's population as provided in RCW 36.70A.040(5), in a county that is planning under all of the provisions of this chapter pursuant to RCW 36.70A.040(5).

(e) Exception. This subsection shall not be interpreted to permit in the rural area a major industrial development or a master planned resort unless otherwise specifically permitted under RCW 36.70A.360 and 36.70A.365.

(6) A transportation element that implements, and is consistent with, the land use element.

(a) The transportation element shall include the following subelements:

(i) Land use assumptions used in estimating travel;

(ii) Estimated traffic impacts to state-owned transportation facilities resulting from land use assumptions to assist the department of transportation in monitoring the performance of state facilities, to plan improvements for the facilities, and to assess the impact of land-use decisions on state-owned transportation facilities;

(iii) Facilities and services needs, including:

(A) An inventory of air, water, and ground transportation facilities and services, including transit alignments and general aviation airport facilities, to define existing capital facilities and travel levels as a basis for future planning. This inventory must include state-owned transportation facilities within the city or county's jurisdictional boundaries;

(B) Level of service standards for all locally owned arterials and transit routes to serve as a gauge to judge performance of the system. These standards should be regionally coordinated;

(C) For state-owned transportation facilities, level of service standards for highways, as prescribed in chapters 47.06 and 47.80 RCW, to gauge the performance of the system. The purposes of reflecting level of service standards for state highways in the local comprehensive plan are to monitor the performance of the system, to evaluate improvement strategies, and to facilitate coordination between the county's or city's six-year street, road, or transit program and the department of transportation's six-year investment program. The concurrency requirements of (b) of this subsection do not apply to transportation facilities and services of statewide significance except for counties consisting of islands whose only connection to the mainland are state highways or ferry routes. In these island counties, state highways and ferry route capacity must be a factor in meeting the concurrency requirements in (b) of this subsection;

(D) Specific actions and requirements for bringing into compliance locally owned transportation facilities or services that are below an established level of service standard;

(E) Forecasts of traffic for at least ten years based on the adopted land use plan to provide information on the location, timing, and capacity needs of future growth;

(F) Identification of state and local system needs to meet current and future demands. Identified needs on state-owned transportation facilities must be consistent with the statewide multimodal transportation plan required under chapter 47.06 RCW;

(iv) Finance, including:

(A) An analysis of funding capability to judge needs against probable funding resources;

(B) A multiyear financing plan based on the needs identified in the comprehensive plan, the appropriate parts of which shall serve as the basis for the six-year street, road, or transit program required by RCW 35.77.010 for cities, RCW 36.81.121 for counties, and RCW 35.58.2795 for public transportation systems. The multiyear financing plan should be coordinated with the six-year improvement program developed by the department of transportation as required by **RCW 47.05.030;

(C) If probable funding falls short of meeting identified needs, a discussion of how additional funding will be raised, or how land use assumptions will be reassessed to ensure that level of service standards will be met;

(v) Intergovernmental coordination efforts, including an assessment of the impacts of the transportation plan and land use assumptions on the transportation systems of adjacent jurisdictions;

(vi) Demand-management strategies;

(vii) Pedestrian and bicycle component to include collaborative efforts to identify and designate planned improvements for pedestrian and bicycle facilities and corridors that address and encourage enhanced community access and promote healthy lifestyles.

(b) After adoption of the comprehensive plan by jurisdictions required to plan or who choose to plan under RCW 36.70A.040, local jurisdictions must adopt and enforce ordinances which prohibit development approval if the development causes the level of service on a locally owned transportation facility to decline below the standards adopted in the transportation element of the comprehensive plan, unless transportation improvements or strategies to accommodate the impacts of development are made concurrent with the development. These strategies may include increased public transportation service, ride sharing programs, demand management, and other transportation systems management strategies. For the purposes of this subsection (6) "concurrent with the development" shall mean that improvements or strategies are in place at the time of development, or that a financial commitment is in place to complete the improvements or strategies within six years.

(c) The transportation element described in this subsection (6), and the six-year plans required by RCW 35.77.010 for cities, RCW 36.81.121 for counties, RCW 35.58.2795 for public transportation systems, and **RCW 47.05.030 for the state, must be consistent.

(7) An economic development element establishing local goals, policies, objectives, and provisions for economic growth and vitality and a high quality of life. The element shall include: (a) A summary of the local economy such as population, employment, payroll, sectors, businesses, sales, and other information as appropriate; (b) a summary of the strengths and weaknesses of the local economy defined as the commercial and industrial sectors and supporting factors such as land use, transportation, utilities, education, workforce, housing, and natural/cultural resources; and (c) an identification of policies, programs, and projects to foster economic growth and development and to address future needs. A city that has chosen to be a residential community is exempt from the economic development element requirement of this subsection.

(8) A park and recreation element that implements, and is consistent with, the capital facilities plan element as it relates to park and recreation facilities. The element shall include: (a) Estimates of park and recreation demand for at least a ten-year period; (b) an evaluation of facilities and service needs; and (c) an evaluation of intergovernmental coordination opportunities to provide regional approaches for meeting park and recreational demand.

(9) It is the intent that new or amended elements required after January 1, 2002, be adopted concurrent with the scheduled update provided in RCW 36.70A.130. Requirements to incorporate any such new or amended elements shall be null and void until funds sufficient to cover applicable local government costs are appropriated and distributed by the state at least two years before local government must update comprehensive plans as required in RCW 36.70A.130.

RCW 43.09.200
Local government accounting – Uniform system of accounting.

The state auditor shall formulate, prescribe, and install a system of accounting and reporting for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

The system shall exhibit true accounts and detailed statements of funds collected, received, and expended for account of the public for any purpose whatever, and by all public officers, employees, or other persons.

The accounts shall show the receipt, use, and disposition of all public property, and the income, if any, derived therefrom; all sources of public income, and the amounts due and received from each source; all receipts, vouchers, and other documents kept, or required to be kept, necessary to isolate and prove the validity of every transaction; all statements and reports made or required to be made, for the internal administration of the office to which they pertain; and all reports published or required to be published, for the information of the people regarding any and all details of the financial administration of public affairs.

APPENDIX H
City Audit Responses

Appendix H contains the responses from each City to the Impact Fees Performance Audit report.

City of Federal Way

- Overall Comment on the Audit
    1. *Small Sample Size*:
       Only 5 entities were selected for this Performance Audit: 4 have traffic fees, 4 have school impact fees, 3 have park impact fees, and 2 have fire impact fees. Given the small size of the audit sampling, the usability of the audit findings and conclusions are limited; therefore, caution should be taken when considering legislative and systematic changes based on the same.

Entity	Impact Fee Collected	Type of Impact Fee
Vancouver	$24.3 million	Transportation, Park, School
Olympia	$7.6 million	Traffic, Fire, Park, School
Maple Valley	$6.3 million	Traffic, School
Redmond	$4.6 million	Traffic, Fire, Park
Federal Way	$1.8 million	School

    2. *Over State Projected Savings*:
       When making general recommendations on systematic or technology changes, the Auditor has not provided cost/benefit analysis of their recommended practices nor have the compared the costs, both acquisition and operating, of their recommendations with current practices. Absent a cost/benefit analysis, cost savings may be overstated.

    3. *Legislate vs. Local Discretion*:
       As part of their recommendation, the Auditor suggested clearer definition in RCW to help local compliance of the state law. Examples are the definition of capital facilities and the definition of separate interest bearing accounts. Federal Way respectfully disagrees with their findings and recommendations in this regard.

Each community is different and will have different set of capital facilities impact by growth that falls within the broad categories provided by the statue. The broad law gives local certain degree of discretion to meet their unique needs while meeting the basic premise of impact fee that "growth pays for growth."

- Audit Area #4 and #5

  The Auditor pointed out that, under state law, impact fees are to be deposited in separate interest bearing accounts. The City agrees. It is also true that all impact fees ultimately managed and controlled by the City for City-owned facilities (traffic, parks, fire, for example) are credited with interest earnings from the date of their receipt until they are spent. The City maintains this practice on all City SEPA-based mitigation fees.

  One are that is not as clear is School Impact Fees. Of the 4 cities collecting the school impact fees (Redmond did not start theirs until 2007, outside the audit period), 2 are not allocating investment interest (Olympia and Federal Way), Vancouver only recently (2005) started allocating interests (they also made retroactive credit to their school district), and only Maple Valley has been allocating interests. But all five cities are allocating investment interests on their internal impact fees. Clearly, there are different interpretations of the statue as to when the responsibility of investing the funds is to begin.

  A. *City Ordinance*:

     The City's ordinance on school impact fees clearly assumes that responsibility starts when the funds are transferred to the District, the owner of these funds. FWCC14-215 (a) states "Impact fee receipts shall be earmarked specially and retained in a special **interest-bearing account established by the district** . . . ", emphasis added.

     FWCC 14-217 (b) further identifies that the account is to be established with the King County treasurer; and (c) clarifies that , for administrative convenience, this fund may be temporarily deposited into a city account and, on a monthly basis, the city will deposit the fund into the district's account.

Because of the provision in the FWCC and the resulting interlocal agreement with the District, the City's books never considered the receipts as "revenue". It holds the funds in a liability account pending the transfer to take place in the following month. In addition, our accounting practice does not consider the School Impact fees as "fund available" for **any** City purposes, including investing.

B. *Actual interest earned on small amount of temporary funds:*

The Auditor stated that the actual interest earned should be the amount credited to the impact fee account ("Cities should not allocate interest based on an interest rate that is not equal to actual interest earned."). The question is: what is the "actual interest earned" and at what cost should the City incur to establish it? The Auditor recognizes the difference that the cities' holding of school impact fee is only temporary and therefore use of Local Government Investment Pool (LGIP) rate is appropriate but ONLY for school impact fees (emphasis is theirs).

Like most government entities in the state, the City's checking account is an interest-bearing account, but the earning rates are lower than the LGIP and interest earned is typically used to offset the banking service fees, with no net interested revenue. Also common to local governments in Washington, the City maintains substantial portion of its cash/investment portfolio in LGIP. Therefore the City's portfolio earning rate is substantially the same as LGIP rate.

The Auditor identifies Vancouver's treasury management software that performs daily interest allocation as the "best practice" and suggests that "the cities should consider procuring the technology, which allows for a daily allocation of interest and minimal manual input." It should be noted that most treasury management software is designed for large entities with a substantial investment portfolio. While the interest allocation and posting may not require manual intervention, the maintenance of system data would. Therefore, it is uncertain how much overall staff time cost/saving one may realize by using such a system vs. using a simple spreadsheet-based interest revenue allocation system. It probably depends on the cities' investment practice. It is also questionable whether the daily revenue allocation would be practical. The bottom line is regardless how complex a system we use to allocate interest earning, as long as the investments are pooled, allocated to of earnings to the various impact fee accounts are "approximations" and would never be "actual" earnings. The alternative of maintaining separate bank accounts (which the Auditor also suggests, absent of legislative change), would likely to result in even more cumbersome and more costly treasury management and less efficient and less cost effective for all parties concerned.

In conclusion, the City does not have any problem with allocating or remitting retroactive and future interest on school impact fees to the school district. [Note: The City has since remitted all past interest and started allocating and remitting current interest to the school district.] However, the City disagrees with the Auditor in applying the statute to the City when the City's role in the fee collection process is temporary custodian or agent as evidenced by the City Code and demonstrated in the City's accounting of the funds. If we apply the Auditor's rational to other restricted revenues, the City should receive interest earning in many revenues that are collected by the state and/or county on behalf of the City, such has Real Estate Excise Tax and Lodging Tax.

- <u>Audit Area #7</u>

  The Auditor only reviewed the school impact fee schedule/calculation reviewing process for the cities of Vancouver and Olympia. They documented Vancouver's review process that includes planning staff, planning commission review, public hearing, and City Council adoption. They did not provide detailed information of Olympia's process, but only indicated it is "lighter". From this limited review, it was determined that "*Cities may not perform a detailed review of a district's CFP or impact fee calculations.* . . ."

  The City of Federal Way reviews Federal Way School District's Capital Facilities Plan for the assumptions, sampling data, and fee calculation and works with District staff to make necessary adjustments/corrections before presenting the results and recommendations to the City Council committee review and then to full Council for adoption.

FWCC provides clear guidelines for annual school impact fee elements and calculations.

- Audit Area #9

  Ernst & Young reviewed permit systems of 3 cities: Vancouver, Olympia, and Redmond. Their finding states that Vancouver and Olympia, which have their permit systems integrated with their GL systems, are Best Practices.

  The Auditor further describes the interface between Vancouver's Tidemark permit system and the Oracle-based GL accounting system as follows:

  - *A customer comes to the permit office to pay the impact fees due and obtain a building permit.*
  - *A permit technician (one who works at the city and issues permits) logs into Tidemark to pull up the building permit application for the customer.*
  - *The permit technician enters the building permit data. The impact fee data is automatically calculated in the system based on the type of land use (i.e., multi-family, single-family, retail, etc.), the building site address, and the square footage (if necessary). Manual entry (i.e., override) of the impact fee is possible, but not generally utilized, except for single-family transportation impact fees. Ernst & Young noted that there is no review or approval of the overrides.*
  - *Once all building permit data is entered, an impact fee amount is automatically calculated in Tidemark.*
  - *The customer then pays a cashier the amount of impact fees owed.*
  - *The cashier receives the monies paid against the amount owed in Tidemark, and the building permit is issued.*

  Ernst & Young noted that Tidemark is fully integrated with the city's GL system, Oracle. Each day the Vancouver Accounting Department logs into Oracle and pulls the report generated by Tidemark for the previous day. The report is uploaded into Oracle. The Accounting Department performs a reconciliation of the data between Oracle and Tidemark to determine that all information transferred correctly."

  Federal Way would like to point out that our permit system and GL system have the same interfaces as described above. We do not consider them fully integrated. It has been a long-term goal for the City to have its many applications fully integrated with the GL system to eliminate the need for reconciliations and data download/upload between systems. However, when the total acquisition and staff support time considered, a fully integrated, enterprise-wide system is not always the best solution for all organizations, particularly the smaller the entities.

City of Maple Valley

- Audit Area #8:

  1. Maple Valley does implement a construction cost adjustment to keep transportation impact fees in line with the cost of projects they fund. The City updates the projects cost annually as part of updating Six-Year TIP. Maple Valley utilizes the adjustment rates provided by WSDOT.

  2. City of Maple Valley has adopted a transportation impact fee schedule in its ordinances that allows a developer to determine the impact fee to be paid upon building permit issuance. City of Maple Valley suggest using Institute of Transportation Engineers (ITE) Trip Generation manual. This manual is widely used throughout United States.

City of Olympia

- General Comments

  First, the Draft Audit lacks clarity concerning its audit objectives. The Auditor's Office has consistently confirmed that the performance audit on impact fees does not make findings concerning legal compliance and in fact reviews performance in certain areas by applying standards that go beyond the applicable legal requirement. The Draft Audit only minimally acknowledges these additional requirements and fails to clearly acknowledge the limitations in its findings. As such, the Draft Audit fails to provide the level of clarity that is expected in an audit performed by the State Auditor.

  The Auditor promises through materials on his website that an auditee is entitled to expect a "clear explanation of the audit's scope and objectives." The Draft Audit, however, does not clearly state that its performance objectives exceed legal requirements, despite what the City believed was a commitment to include language in the Draft Audit to clarify this point. The Draft Audit should be revised to clarify the scope of a performance audit, the areas in which the performance audit includes objectives that exceed legal requirements, and the limitations inherent in certain findings.

As noted on the Auditor's web site, a performance audit looks either at "the extent to which a program is achieving its goals and objectives" or "whether an entity is acquiring, protecting and using its resources in the most productive manner to achieve program objectives." In an audit such as this, where the Audit staff creates objectives that exceed legal requirements, it is critical that the audit's scope and objectives are clearly discussed.

Second, the City notes that, although we were hopeful that the performance audit would provide us with suggestions and best practices that would lead to new efficiencies and result in real cost savings, we can identify no such practices for the City of Olympia.

- Audit Area #3:

  The Draft Audit fails to fully explain the basis for one of the "performance" objectives it attempts to measure. Performance audits evaluate the "economy, efficiency and effectiveness" of local government programs. In light of the purpose of performance audits and materials on the Auditor's website, the "program objectives" selected for measurement in an audit arguably should be selected from objectives set for the entity by the state Legislature or local elected officials. One of the objectives applied in the Draft Audit, however, seeks to measure whether cities have attained performance standards that are beyond what is required by state or local laws. In reviewing park impact fees, the Draft Audit attempts to evaluate how local governments demonstrate a close geographical connection between where impact fees are collected and spent, despite Audit staff's acknowledgement that the Legislature did not require the "close connection" the Draft Audit seeks to measure.

  The Draft Audit's minimal acknowledgement that this new "close connection" standard goes beyond what is required by law is inadequate in light of the complexity of the issue. Moreover, the Draft Audit fails to recognize that the manner in which this new measurement standard is applied to Neighborhood Park Impact Fees effectively second-guesses the legislative determination made by the Olympia City Council concerning the appropriate service area of neighborhood parks.

Local elected officials have considerable discretion in the area of planning for new growth and development and setting impact fees. The manner in which the new measurement standard is applied in the Draft Audit is inconsistent with the authority granted by state law to local elected officials. Olympia's City Council has determined that a single zone for neighbor parks is an appropriate reasonable service area. This determination was based on sound planning principles. The Draft Audit acknowledge that the Council's determination is consistent with the statutory requirements, and yet it inexplicably proceeds to add an additional measurement beyond what is legally required and uses this extra measurement to question a policy decision made by Olympia's legislative body.

Finally, the Draft Audit applies its new measurement standard to Park Impact Fees without any analysis as to whether the new standard will create inefficiencies as opposed to the efficiencies a performance audit is expected to identify. The Draft Audit acknowledges that cities such as Olympia have legitimate reasons for using a single zone, including certain efficiencies created by a single zone. The Draft Audit, however, inexplicably recommends that Olympia consider implementing multiple zones in order to achieve an objective created by the Audit staff that goes beyond legal requirements without any analysis as to how multiple zones could impact Olympia's system.

The lack of acknowledgement in the Draft Audit that its recommendation may well create inefficiencies rather than efficiencies is problematic. This is especially so where the potential inefficiencies created by the recommendation may make it more difficult for Olympia to achieve the purposes of the impact fee statute.

- <u>Audit Area #6</u>

  In criticizing Olympia's Fire Impact Fee, the Draft Audit applies an overly narrow approach to impact fee calculation. The Draft Audit appears to be based on the concept that impact fees must be derived from an "improvements driven methodology" that expressly mentions the cost of new fire facilities and certain other components. The Draft Audit further compounds its errors by inappropriately applying data from Redmond to estimate an amount Olympia possibly could have charged in impact fees under an improvements driven approach. The analysis not only uses data that does not apply, but also is based on a more limited scope of projects than are identified in Olympia's Comprehensive Plan.

Local governments have considerable discretion in the calculation of impact fees. Olympia's calculation formula "incorporates" the components set out in state law through a "standards-driven" methodology that incorporated the costs of needed future facilities as determined by the costs of demonstrably less expensive, existing facilities. This approach complied with applicable requirements. Moreover, a reasonable conclusion would be that it actually resulted in impact fee rates that substantially *undercharged* for the needed new facilities.

The Audit staff is aware that Olympia is in the process of designing and constructing a new Fourth Fire Station due to growth in service demands and increases in population. Information was provided showing that the land and construction costs for this single project are projected to be nearly $8 million, whereas Olympia has collected less than $2 million in Fire Impact Fees. In addition, Olympia recently obtained voter approval of a levy lid lift to pay for the uncovered costs of constructing the new fire station. Accordingly, the Draft Audit should clearly acknowledge that Olympia may have *undercharged* Fire Impact Fees using its current calculation method. Finally, the calculation that misapplies Redmond's data in an attempt to recalculate Olympia's potential impact fees should be removed. This calculation does not further the discussion concerning the difference between impact fee calculation methods and is potentially misleading. While the City agrees that it is time to revisit its Fire Impact Fee calculation, the decision on the method to be used in its fee calculation is within the discretion afforded local officials.

- <u>Audit Area #5:</u>
  The Draft Audit relies upon an overly literal reading of RCW 82.02.070 to justify its findings relating to School Impact Fee accounting and interest. The Draft Audit applies a literal statutory reading to justify recommendations that cities implement expensive, automated daily interest allocation software. Moreover, although Audit staff acknowledged the efficiency of an agreement between the City and the District allowing the City to retain minimal interest amounts to offset the cities' administrative impact fee collection costs, the Draft Audit persists in recommending that Cities remit this small

amount of interest. The performance audit has identified no fraud or error in interest calculation and does not dispute that collection of the impact fees facilitates the construction of capital facilities for which the fees were imposed. The cities' collection efforts are part of the purpose of the impact fees, and the use of interest from those fees to offset administrative costs associated with the fee collection should be considered legitimate. Although the City disagrees with the Draft Audit's analysis, the City will modify its arrangement with the District and remit interest effective August 2008.

City of Redmond

No response provided.

City of Vancouver

- Audit Area #8:

  The City's current Transportation Impact Fee Program fully complies with all the recommendations made within the report. A fee schedule is adopted yearly by ordinance and is referred to in VMC 20.915.040 as the TIF Program Technical Document. The technical document is published and developers can readily access it and use it to calculate their fee. We believe that this aides in our strong customer service focus when working with our local developers.

- Audit Area #9:

  We will be increasing our permit system capabilities in order to reduce the need to manually override fees. Should instances arise that require a manual override, we will be reviewing those situations to determine that they are valid and accurate. Finally, we will be continuously monitoring the access granted to users of the system. We believe these steps will serve to enhance the programs and our already strong system of internal controls.

APPENDIX I
Ernst & Young's Responses

Appendix I contains Ernst & Young's response to each of the City's responses in Appendix H to the Impact Fees Performance Audit report.

City of Federal Way
No response.

City of Maple Valley
No response.

City of Olympia

- <u>Audit Area #3:</u>
  As noted in the report under the section entitled "Vancouver's rationale for multiple park zones," there are disadvantages to using multiple park zones.

- <u>Audit Area #6:</u>
  In our recommendation we outline that the City should more effectively address RCW 82.02.050 and 82.02.060 in its calculation and demonstrate that the fire impact fee charged reasonably relates to system improvements that are reasonably attributable to growth. Because the City did not have an updated CFP that directly tied its impact fee calculation there are multiple answers as to what the Cities impact fees collected should be as outlined in the report.

  In the report under "Potential Cost Savings and Other Impacts" of Audit area 7 we commented that it is possible that the City may have undercharged, rather than overcharged the fire impact fee given the new $7.9 million fire station the City is preparing to build. We tried several means to determine what the undercharge might have been if a different fire impact fee calculation that tied the impact fee to the CFP were used. During this process we received insufficient data to determine what percentage of the proposed $7.9 million fire station was due to new growth. Data received included, but was not limited to, population growth estimates from 2000 to 2007 of 4%, a 36.8% increase in fire/aid calls for District 4 (the district for which the new fire station is proposed), and construction permits.

City of Redmond
No response.

City of Vancouver
No response.

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