



CITY OF KIRKLAND
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MEMORANDUM

To: David Ramsay, City Manager

From: Marilynne Beard, Assistant City Manager
Tracey Dunlap, Director of Finance and Administration

Date: February 18, 2009

Subject: 2009 Annexation Update

Introduction/Purpose of the Update

On April 15, 2008, the City Council decided to suspend deliberations related to the Potential Annexation Area (PAA) until the financial challenges of the 2009-2010 budget were addressed. With the adoption of the budget on December 16, 2008, staff began the process of updating the annexation financial model to determine the impacts of the 2009-2010 budget decisions on the annexation fiscal picture. The update presents two scenarios:

- A "base case" for annexation that assumes the "Alternative Service Delivery" scenario last discussed on 4/15/08, updated to reflect more recent financial assumptions, and
- An alternative that reflects the original service delivery assumptions for the public safety functions.

In addition, a number of contingencies based on various economic and policy outcomes have been identified in terms of potential positive/negative impacts to assist in determining the risks/benefits associated with annexation. These contingencies can be added to or subtracted from the two scenarios presented to provide context for the policy evaluation of different annexation assumptions.

Updated Financial Model

Background

At the end of the first phase of the annexation analysis (late 2006/early 2007), the financial model projected that there was a financial gap in both the existing City and the PAA. The gaps were roughly proportionate and scenarios were generated that illustrated potential actions that would close the gap. These scenarios indicated that the actions taken to close the gap in the existing City would also close the gap in the PAA.

In late 2007, the financial results were updated to take into account new information, including:

- The adopted 2007/08 budget,

- The costs of adding a fire engine company due to the expected relocation of the Kingsgate fire station,
- The costs of maintaining O.O. Denny Park if the Finn Hill Park District dissolved,
- Assumption of the anticipated Fire District 41 debt associated with station consolidation, and
- Updated facilities cost estimates.

These changes added sufficient costs to the PAA that the logic that the actions taken to balance the existing City's budget would balance the PAA no longer held true. To further evaluate the financial feasibility of annexation, the City Council requested that options be generated for consideration that included an Alternative Service Delivery (ASD) approach for the PAA that would reduce costs.

In April 2008, the Alternate Service Delivery approach for serving the entire PAA was presented that reflected the following key changes:

- Assumption that the City will not assume responsibility for O.O. Denny Park,
- Adjustment to Police patrol districts from 4 to 3 in the PAA,
- Change in minimum Fire staffing configuration, and
- Overall reduction in staffing needs of approximately 20.7 FTEs (13 percent).

These service level adjustments produced a gap in the PAA that is roughly proportionate to the gap in the existing City, which returned the discussion to the earlier logic – that the actions taken to balance the budget in the existing City should also balance the PAA.

The 2009 update reflects the following changes since the April 2008 analysis:

- Incorporated the 2009-2010 Adopted Budget decisions, including the increases in the business license fee and public and private utility taxes, expenditure reductions, transition to NORCOM, and changes in the City's fund structure,
- Reduced in baseline sales tax due to no growth in receipts from 2006 to 2007, a 9% decline in 2008, and recognizing the impacts of the new Redmond Costco store and relocation of Toyota of Kirkland from the existing City to the PAA,
- Adjusted near-term existing City land use and development assumptions to better reflect the impacts of the current economic slowdown,
- Changed the first full year that annexation is effective to 2011 to reflect the time that has passed since the last update (was 2010 in the prior analysis),
- Adjusted inflation assumptions to be consistent with the 2009-2010 budget, with a return to more long-term trends beginning in 2012 for wage growth (5%) and benefit growth (6%).
- Removed assumed impacts from the redevelopment of Totem Lake Mall. Given the delays in the project, the current scenario does not include the projected impacts which had been reflected in the previous version beginning in 2011 (see further discussion in the *Contingencies* section later in this document regarding the potential impacts of both the Totem Lake and Park Place redevelopment).

Updated Assumptions

The 2009 model scenarios assume that the City will annex all three areas in the PAA, including the full Kingsgate area. The "base case" reflects the Alternative Service Delivery option

presented at the April 15, 2008 Study Session. The assumptions are similar to those summarized above, with minor updates to the PAA staffing estimates to reflect new input from selected departments and the impacts of the service level reductions. As a reminder, the public safety staffing assumptions under the Alternative Service Delivery approach reflect:

- *Police Patrol Districts* - To achieve staffing economies in the Police Department, the department reduced the number of patrol districts serving the area from four to three. The patrol district boundaries were revised based on the population of each of the districts, projected calls for service within the districts, and the ease of transportation access within the district. Currently, the police department handles just under 38,000 calls for service (incidents) each year. These calls for service include both when the officer is dispatched to an incident by the Dispatch Center and when the officer observes a potential incident and initiates a response. These incidents include traffic stops, arrests, and on-view contacts. Based on historical data, the department projects approximately 26,000 calls for service (incidents) each year in the PAA. Approximately one-third of these calls will require a minimum of two officers to sufficiently handle the call (such as domestic violence calls).

The revised boundaries for the three patrol districts in the PAA reflect the geographic constraints associated with the area. The challenges include the lack of east to west arterials and the high volume of traffic on north-south arterials and I-405. In addition, NE 132nd Street is the one clear direct route for officer response from one district to another. The map in Attachment A illustrates the proposal for the three patrol district boundaries.

- *Fire Staffing Configuration* - The alternative service delivery plan includes a proposed change to the current firefighter staffing requirements for the Totem Lake station. Currently, the Fire Department requires a total of five positions to staff an engine company and a medical aid unit -- three firefighters for the engine company and two for the medical aid unit. This reflects a service level enhancement approved several years ago that allows for the Totem Lake Station to respond to two separate aid calls simultaneously or one fire and one aid call simultaneously. Under the alternative service delivery plan, the Totem Lake Station would be reduced to a total of four staff that have the flexibility to work as part of either the engine company or the aid unit. The station would be equipped with both an aid vehicle and a fire engine.

With this level of staffing, the station personnel retain the ability to respond to two medical emergency calls at the same time or one fire call. Also, it gives the station the ability to staff an engine company with four firefighters in the event of a fire emergency, giving the team greater capacity to handle fire related actions. However, the station staff would require automatic aid assistance to respond to simultaneous medical and fire calls. It should be noted that the Fire Department is considering this change in staffing configuration on a citywide basis because it does offer increased flexibility in staffing. This alternative staff configuration at the Totem Lake Station would result in an overall reduction in three staff positions—one for each of the three shifts needed for 24/7 coverage.

For the alternative case, the Public Safety staffing levels are returned to the earlier service levels assumptions, specifically four Police Patrol Districts and the independent Aid Car staffing

model in Fire. Both scenarios assume that OO Denny Park maintenance will continue to be done by the Finn Hill Park District.

Financial Outcomes

The "Base Case" results reflect the Alternative Service Delivery assumptions. The projected core expenditures in the PAA are lower than in the previous analysis due to a number of factors:

- The current escalation of salaries and benefits from 2008-2011 is lower than that projected earlier by the model;
- Development assumptions were reduced in the early years of the projection to reflect current economic conditions, which results in slower growth in related staffing;
- The earlier model assumed growth in FTEs between 2008 and 2011, which was higher than what actually occurred;
- Other adjustments due to updating the assumptions to the 2009-2010 budget related to hourly labor and the relationship of labor costs to non-labor costs.

Similarly, the revenues in the PAA have increased since the last update due to the increases in utility tax rates and the revenues from the relocation of the Toyota dealership to the Graham Steel site; however, a significant portion of these increases have been offset by lower sales tax collection assumptions, reductions in development activity, and reduced property tax growth.

The results show that the 2009-2010 budget decisions, particularly the increase in utility taxes, have improved the financial results in the PAA better than in the existing City. This is based, in part, on the fact that utility taxes are a much larger share of the revenues in the PAA than they are in the existing City. The actions taken to balance the budget in the future in the existing City would work as well or better in balancing the PAA.

The "Alternative Case" results reflect higher FTE assumptions for Police and Fire (13 additional public safety FTEs). In this case, the shortfall in the PAA is larger than that in the existing City, so that the budget-balancing actions for the existing City would not balance the PAA until much later in the projection period.

The table on the following page summarizes the results for both scenarios. The ASD model results from April 15, 2008 are provided for context in Attachment B. The model summary sheet for the "base case" is included as Attachment C and the "alternative case" is shown in Attachment D.

Summary of Overall Results (Dollars in thousands)

Alternative Service Delivery (3 District) - "Base Case"

	2011	2016	2021	2026
<i>Current Kirkland</i>				
Net Resources	\$ (4,369)	\$ (6,916)	\$ (11,936)	\$ (18,003)
(Deficit)/Surplus as % of Expenditures	-7%	-8%	-11%	-13%
<i>Potential Annexation Area (PAA)</i>				
Net Resources	\$ (1,609)	\$ (1,383)	\$ (2,048)	\$ (858)
(Deficit)/Surplus as % of Expenditures	-10%	-6%	-7%	-2%
<i>Total (Current City & PAA)</i>				
Net Resources	\$ (5,978)	\$ (8,299)	\$ (13,983)	\$ (18,861)
(Deficit)/Surplus as % of Expenditures	-7%	-8%	-10%	-10%

Restored Service Level (4 District) - "Alternative Case"

	2011	2016	2021	2026
<i>Current Kirkland</i>				
Net Resources	\$ (4,365)	\$ (6,912)	\$ (11,931)	\$ (17,997)
(Deficit)/Surplus as % of Expenditures	-7%	-8%	-11%	-13%
<i>Potential Annexation Area (PAA)</i>				
Net Resources	\$ (3,128)	\$ (3,841)	\$ (5,183)	\$ (4,864)
(Deficit)/Surplus as % of Expenditures	-17%	-15%	-16%	-11%
<i>Total (Current City & PAA)</i>				
Net Resources	\$ (7,494)	\$ (10,753)	\$ (17,114)	\$ (22,861)
(Deficit)/Surplus as % of Expenditures	-9%	-10%	-12%	-12%

To provide a different perspective, we have rearranged the PAA results of the two scenarios in the table below to compare "core resources" to "core expenditures", which essentially indicates the balance between operating sources and uses (excluding facilities and the state sales tax credit). The table shows both the operating balance, as well as the overall balance.

Summary of Model Potential Annexation Areas (PAA) Results

Alternative Service Delivery (PAA Only) - "Base Case"

	2011	2016	2021	2026
Core Expenditures	\$ 16,786	\$ 23,096	\$ 29,959	\$ 38,457
Core Revenues	\$ 17,316	\$ 22,028	\$ 28,986	\$ 38,698
Core Net Resources	\$ 530	\$ (1,068)	\$ (973)	\$ 241
Facilities Cost	\$ 6,379	\$ 6,370	\$ 1,075	\$ 1,099
State Sales Tax	\$ 4,240	\$ 6,055	\$ -	\$ -
Total Net Resources	\$ (1,609)	\$ (1,383)	\$ (2,048)	\$ (858)

Restored Public Safety Level of Service (PAA Only) - "Alternative Case"

	2011	2016	2021	2026
Core Expenditures	\$ 18,304	\$ 25,554	\$ 33,094	\$ 42,462
Core Revenues	\$ 17,315	\$ 22,028	\$ 28,986	\$ 38,697
Core Net Resources	\$ (989)	\$ (3,526)	\$ (4,108)	\$ (3,765)
Facilities Cost	\$ 6,379	\$ 6,370	\$ 1,075	\$ 1,099
State Sales Tax	\$ 4,240	\$ 6,055	\$ -	\$ -
Total Net Resources	\$ (3,128)	\$ (3,841)	\$ (5,183)	\$ (4,864)

Service Level Outcomes

One of questions raised based on the alternative service delivery option is how we can provide differing levels of service between the existing City and the PAA. There are certain services where the impacts of service delivery could likely be contained to the PAA, although the long-term goal would be to levelize services throughout the City over time. For example, the Parks Department could establish a level of parks maintenance for the parks in the annexation area that differs from the level that is provided to current City parks. Although that service level would likely represent an improvement over the level of service that is currently provided by King County, the PAA parks could be maintained at a lower level of service for an indefinite period of time. Similarly, it would take longer to complete neighborhood plans for the PAA and it may take longer to respond to requests for neighborhood traffic calming in that area.

There are other services where it would be difficult to distinguish the level of service impacts between the existing City and the PAA. For example, it would be challenging and undesirable to treat customers coming into City Hall for permit services or planning information differently depending on whether their project was in the PAA or existing City. The City would likely respond to a report of a pot hole in the same manner, regardless of its location, given the liability implication of not fixing the problem. Kirkland staff prides itself on providing good customer service and would find it difficult to differentiate between customers at the counter or on the phone.

Staffing levels in the Police Department provide an established level of response to calls for service. Any call that is a report of a "crime in progress" (e.g. domestic violence, burglary, auto theft) requires more than one officer to respond to ensure officer safety. This means that a car from one patrol district must leave their assigned area to assist another officer. Officers in other patrol districts then cover calls for service in the area left unmanned. This already occurs on a regular basis within Kirkland with officers moving between patrol districts for back-up. In fact, Kirkland officers currently provide back-up service to the King County Sheriff's Office in the PAA, thereby reducing coverage within the current City limits during the back-up engagement.

The Police Department projects that the PAA will generate approximately 26,000 annual calls for service. There will be some service impacts to both the existing City and the PAA associated with adopting a three district plan, but these impacts should be manageable. The response in the PAA should still represent a significant improvement from King County and the system will be designed with the objective of managing any impacts in the existing City. The most noticeable result of the three-district plan would be the need to have a more refined system of prioritizing calls for service. The response to life-threatening or in-progress crimes will be enhanced in the PAA. However, lower priority calls may likely to have longer response times than is current practice within the City. Another impact of adopting a three-district plan would be the increased demand for backup support. Specifically, we anticipate that there will be an increase in the need for current City officers to assist the PAA officers with backup emergency calls. To manage this demand for assistance, the boundaries of the current north districts borders would be redrawn to aid in reducing the work load and coverage area in these districts. Doing this reduces the area and population in the north districts and gives this area to the two remaining south districts. This should spread the impact of increased calls to all districts and would be monitored for issues. Under a three district plan, there will be an increased number of hours where a command staff person is on duty, but there will still be times during weekends or late evenings when a sergeant or corporal is the highest ranking staff member.

Listed below are several impacts of reducing the number of districts and staff covering the PAA. Emergency assistance and the preservation of life would always be our top priority. As mentioned above, the Police Department's greatest challenge will be in providing a standard level of service for lower priority response calls. Some of the possible methods of prioritizing and handling the additional calls for service include:

1. Limiting the types of calls officers are required to handle (e.g. non follow-up calls handled as mail out reports, raising the dollar threshold on reporting non-injury accidents, barking dog complaints and others).
2. Offering internet-based reporting by victims; easy to use question/answer templates for reporting non follow-up case types which allow officers to be available for other calls. This can be done on the internet, by setting up a reporting station at various locations in the City (fire stations, police department, and community center).
3. Working a different schedule with patrol that allows for different staffing levels for peak times. In the past, the twelve-hour work schedule limited scheduling flexibility. Effective February 16, 2009, the City and the union agreed to change to a more flexible scheduling plan that should assist with this issue.

As described earlier, the change in the Fire staffing model retains the ability to respond to two medical emergency calls at the same time or one fire call. Also, it gives the station the ability to staff an engine company with four firefighters in the event of a fire emergency, giving the team greater capacity to handle fire related actions. However, the station staff would require automatic aid assistance to respond to simultaneous medical and fire calls.

Contingencies

Voted Utility Tax - The 2009-2010 Budget assumes passage of a voted utility tax increase on private utilities of 1.5%, which is reflected in the base case. This assumption is one of the key factors in the improvement of the PAA projection, as utility tax is one of the largest revenue sources in the PAA. Voter rejection of the measure represents a potential annual downside risk of \$2.3 million for the existing City in 2011 and \$1.1 million for the PAA in 2011, or a total annual revenue risk starting at \$3.4 million and growing over time.

Impacts of Current Economic Environment – The primary risks associated with the current economic environment involve additional losses of sales tax revenue and lower than expected development activity. The model scales development-related staffing to match development revenues (at the appropriate cost recovery level), so a lower level of development revenue would also result in lower costs of development-related staffing.

In terms of sales tax, lower sales tax collections impact the existing City much more severely than the PAA. The projected sales tax in 2011 generated by the existing City is \$15.0 million, so a 1% decline in taxable retail sales would result in a loss of \$150,000. In contrast, the projected sales tax in the PAA in 2011 is \$1.8 million, so a 1% decline equates to \$18,000. Given that sales tax is a much smaller part of the PAA tax base, the risk to the annexation scenario of a decline is much less than the impact on the existing City, so it should not have a significant adverse impact on the PAA outcome.

In terms of the state sales tax credit, each 1% reduction in the combined sales tax revenues decreases the credit by \$42,000 beginning in 2011. To illustrate the impact, the sales tax credit in the April 2008 model (2010) was \$4.9 million and the 2011 credit is currently \$4.2 million. Further description of the state sales tax legislation and pending bills is provided later in this report.

While data is not available to determine the impact of streamlined sales tax on the PAA revenues, given that sales tax is not a major revenue driver, we recommend no adjustment to recognize potential impacts.

Totem Lake Mall – Prior versions of the annexation model assumed that redeveloped Totem Lake Mall would be completed by 2011. Given the delays that have occurred in commencement of the project and the current economic climate, this update does not assume a completion date for redevelopment of the mall. If the mall is redeveloped under the original assumptions underlying the development agreement in 2006, the net revenue generated by the project (after debt service on the public facilities) was projected at \$410,000 when construction was complete in 2011 and growing thereafter. Recent discussions have indicated that there may be changes in the design that would reduce the net revenue by as much as \$340,000, generating an initial net revenue to the City of \$70,000. Once the final scope and funding of the project is known, the cash flow projections supporting the development agreement will need to be revisited to assess the net benefits of the project.

Park Place – With the approval of the zoning changes related to the redevelopment of Park Place in December 2008, the design review process is about to get underway. The current schedule contemplates the early stages of construction beginning as early as 2010. The final configuration of the development is not yet known, however, preliminary financial analysis estimates that the redeveloped area would generate a net annual revenue to the City of \$560,000 when the project is completed in 2014 (after funding of the direct impacts).

Gambling Tax Revenue – The Caribbean Casino operates in the Kingsgate area and contains a social card room that is prohibited under Kirkland's current zoning. Since the model was last updated, the gambling taxes paid to King County by the casino have increased significantly, from the 2006 figure of \$580,000 to a 2008 figure of \$820,000. King County's gambling tax rate is 11%. The City currently has a higher rate on social card games of 20% (although they are prohibited in the City limits). If this rate were applied to the 2008 receipts, the revenue would be \$1.49 million. However, this figure assumes that the higher City of Kirkland rate of 20% would be applicable to all revenue, although a more likely scenario is a blended rate that more closely reflects the actual activities being taxed (for example, Kirkland's rate for bingo, raffles, etc. is 5%). It would be prudent to assume conservative potential revenue in the range of \$800,000 (assuming the King County rate of 11%) to \$1.2 million (recognizing the City's higher rate for card rooms, but factoring in that it would not apply to all revenues). See the legislative update later in this memo for an update on pending legislation to allow such uses to be "grandfathered" upon annexation.

Flood Control Zone District – The King County Flood Control Zone District (KCFCZD) was created in 2008 with the purpose of addressing major-river flooding problems that impact the regional economy. In establishing the KCFCZD, the Board of Supervisors set aside 1 cent of the 10 cents per \$1,000 of assessed value levied for a sub-regional opportunity fund to address local flooding problems unrelated to large rivers. Approximately \$53,000 per year will be allocated to the Kirkland PAA that includes Juanita, Kingsgate and Finn Hill areas (there is

currently \$106,000 that would be allocated to King County as of January 1, 2009). The actual amount available will vary slightly based on assessed property value in the area, and on actual payments received. The levy will be collected for 10 years, and can be renewed. The amount of the levy can be adjusted downward, but cannot be adjusted upwards without voter approval.

These revenues could be used for flood control, stormwater and cooperative watershed management actions, as long as such actions are performed under a comprehensive plan, which means this revenue would be applied to the stormwater utility. While the stormwater utility is not included in the fiscal model, we wanted to acknowledge that we will receive an additional share of the Flood Control Zone District funding if we annex the PAA.

Regional Jail - The City's investment in and use of a regional jail facility will be under study for at least another year before we can determine our level of participation in the project. However, initial projections (for the existing City only) indicate that the incremental annual cost increase due to new bed-day costs, assuming the City continues to operate a 12-bed facility, would be \$670,000. Based on the 2007 Jail Staffing study, the PAA would increase the bed-days by approximately 50%, increasing the PAA cost by as much as \$335,000.

Fire Station Consolidation Debt - The financial model assumes that the City of Kirkland will assume responsibility for debt issued by Fire District #41 for the station consolidation, estimated at \$290,000 per year in the model. The economic stimulus package includes a provision for competitive "firefighter assistance grants" of up to \$15 million for modifying, upgrading, or constructing State and local fire stations. If the station consolidation qualifies for this program, it could eliminate the need to issue new debt to finance the project.

Facility Expansion Options - At the January 6, 2009 meeting, Council asked staff to explore options for facilities expansions. A significant expense included in the original financial model related to the construction of a new public safety facility and improvements needed to City Hall and to the Maintenance Center to accommodate new staff. Council asked staff to determine whether it is possible to construct a new public safety facility on the existing City Hall site in order to avoid the cost of constructing a new, stand-alone facility that would require acquisition of land and/or an existing building.

Since the original annexation financial model was developed some changes have occurred that affect facilities needs:

- Under the alternative service delivery model, staff projections for annexation were decreased.
- The City's Communications Center will move to NORCOM in July 2009.
- The former Hopelink building is now available for City staff and/or meeting rooms.

After reviewing architect Jim McClaren's original space requirements with facilities staff and the architect, we determined that we could change the assumptions in the study and build on the existing City Hall site. For instance, the original staffing estimates are higher than the most recent staff estimates prepared in 2008. The study assumed a 75-bed, full-service jail. The City is now exploring regional alternatives and has determined that a small full-service jail is not the most cost-effective option. The original design included some spaces that could be located outside of City Hall proper such as a gun range. In addition, one or more departments could remain off-site or relocate to the City Hall Annex (e.g. Parks or Human Resources staff currently located at the 505 Market building).

The downsides of this alternative relate to our ability to expand to meet long term needs and to consolidate public safety functions on one site. However, if the addition to City Hall is constructed to essential building standards (required for public safety facilities such as EOC's and jails) then other functions could eventually be moved off-site to a standard office building. At some point in the future, the City may still build a separate public safety facility. The facilities assumptions assuming no annexation, annexation with a separate public safety facility, and an estimate with annexation but with the public safety facilities located on the City Hall campus (increasing the City Hall project cost) are summarized below.

Estimated Facilities Costs (in 2005 dollars)

Facility Needs	No Annexation	With Annexation (Separate Public Safety Building)	With Annexation (No Separate Public Safety Building)
City Hall Expansion (incl. public safety)	25,000,000	N/A	40,000,000
Public Safety/Jail Building	N/A	38,554,236	N/A
City Hall Space Needs	N/A	28,900,000	N/A
Maintenance Center Space Needs	4,564,000	7,763,000	7,763,000
TOTAL	\$ 29,564,000	\$ 75,217,236	\$ 47,763,000

Annual Facility Debt Service Paid by:	No Annexation	With Annexation (Separate Public Safety Building)	With Annexation (No Separate Public Safety Building)
Existing City	2,482,106	2,576,861	2,576,861
PAA Share of Baseline		1,072,955	1,072,955
PAA Increment	-	5,305,903	2,507,128
TOTAL	\$ 2,482,106	\$ 8,955,719	\$ 6,156,944

The total amount of facility debt service assumed in the financial model is \$2.5 million for the existing City and \$6.4 million for the PAA (during the first ten years), for a total of \$8.9 million, and includes the public safety building, City Hall expansion and Maintenance Center expansion. By eliminating the separate public safety building, debt service could be reduced by up to \$2.8 million for the PAA, depending on how the costs were allocated. This assumption change significantly improves the PAA scenarios, especially during the first ten years.

It should be noted that the state sales tax incentive was largely used to pay facility debt costs so as to mitigate the impact on the operating budget after the ten year eligibility lapsed. If the total PAA budget including facilities does not require the full state sales tax credit amount, then the sales tax credit would be reduced accordingly. Note that the elimination of a separate stand alone building will generate some operating savings, although the extent is difficult to identify with the information currently available.

Note that in December 2007, a variety of financing options were identified as available for the existing City share of facilities expansions (up to \$31 million). While no specific decisions were made, it would be reasonable to include a portion of the resources (approximately \$15 million) toward the existing City's share of the required facilities expansions, which would offset a portion of the debt service costs allocated to the existing City.

King County Funding – In 2007, King County offered the City \$2.5 million in funding, of which \$1.0 million was for capital and \$1.5 million was for general purposes. This offer expired in March of 2008. While it may be unlikely that this level of funding might still be available, staff could pursue some level of funding that could assist with transition costs and/or capital needs.

"Upzoning" Opportunities in Commercial Areas – Work on annexation zoning was not completed when the Council decided to suspend work on annexation in 2008. Staff had finished an extensive comparison of the Kirkland and King County Zoning regulations and prepared draft regulations that would utilize the format and general regulations of the Kirkland code, while creating zoning districts that reflect the development patterns in the annexation area.

There are five commercial districts within the annexation area. The districts all have well established development patterns and, except for the Totem Lake industrial area, they are relatively isolated from other commercial areas. Commercial expansion of all districts is constrained by adjacent single family neighborhoods. Other than Totem Lake, each district primarily provides goods and services to the surrounding neighborhoods. Commercial uses serving a broader market area are more likely to locate in larger business districts with better access – such as Totem Lake.

The Kingsgate, Juanita, North Finn Hill and South Finn Hill districts are developed with a core of commercial uses surrounded by multi-family. Existing zoning reflects this development pattern. The King County Comprehensive Plan, however, does not differentiate between commercial and multi-family. Instead, each of these districts is designated as a "Business Center." In preparing annexation zoning, consideration was given to rezoning some of the Business Center land from multi-family to commercial. This would also involve amending the zoning regulations to allow residential uses on the ground floor of commercial zones in order to prevent existing multi-family uses from becoming non-conforming. Draft zoning maps were reviewed by the City Council as a whole in February 2008 and then by the Council Annexation Subcommittee in April. Based on those meetings, two draft versions of the zoning were created for each business district (see Attachment E). The Annexation Subcommittee version adds additional properties to be rezoned commercial. This would need further review by the full Council if annexation is pursued.

The business area east of Totem Lake is somewhat different than the other neighborhood oriented districts. This area is now zoned Light Industrial and is developed with a variety of uses ranging from auto dealers, to warehouses to offices. The area would be rezoned to correspond to zoning immediately to the west in Kirkland - Totem Lake 7. To better reflect the existing development pattern, a greater range of commercial uses would be permitted.

In summary, there are a number of contingencies that could positively or negatively impact annexation. The table that follows summarizes the range of potential impacts, if available.

Contingency	Potential Annual Impact	
	Failure of the Voted Utility Tax	Existing City
	PAA	\$1.1 million revenue loss
Impacts of Current Economic Environment (Revenue loss for each 1% sales tax decline)	Existing City	\$150,000 revenue loss
	PAA	\$18,000 revenue loss
Impact of 1% Sales Tax decrease on Credit	Combined	\$42,000 revenue loss
Totem Lake Mall Redevelopment (Estimated net revenue gain)	Existing City Only	\$70,000-410,000 revenue gain
Park Place Redevelopment (Estimated net revenue gain)	Existing City Only	\$560,000 revenue gain
Gambling Tax Revenue	PAA Only	\$0.8-\$1.2 million revenue gain
Flood Control Zone District Revenue for PAA (Stormwater Utility revenue/not Gen'l Fund)	PAA Only	\$53,000 revenue gain
Regional Jail Cost Impacts	Existing City	\$670,000 cost increase
	PAA	\$335,000 cost increase
Fire Station Debt Consolidation (If paid by economic stimulus package)	PAA Only	\$290,000 cost decrease
Facilities – No Separate Public Safety Building (Decrease in debt service payment)	PAA Only	up to \$2.8 million cost decrease
King County Funding	PAA Only	unknown
Upzoning Opportunities in the PAA	PAA Only	unknown

Balanced Budget Model

The financial model is intended to provide a long-term projection of the potential financial impacts of annexation, assuming a similar level of service is provided in the PAA and the existing City soon after the effective date of annexation. A different approach to developing an expenditure budget for the PAA is to match expenditures to estimated available revenues, or a "balanced budget" approach. While the model indicates that there will be a shortfall between revenues and expenditures, in reality, the City is required to adopt a balanced budget every two years and will continue to do so.

This "balanced budget" approach would determine the levels of service possible under a scenario where expenditures are matched to the revenues available (balanced budget). The process would mirror a typical budget process, where departments develop their needs and recommended service levels, they are reviewed by the City Manager's Office and prioritized within revenue constraints, and then the resulting balanced PAA budget would be presented to the City Council for consideration. This information would include an articulation of the levels of service as compared to the current City of Kirkland and the current King County standards in the PAA.

It is important to recognize that the state sales tax credit is only available toward costs to provide services in the PAA that are in excess of revenues generated. The scenarios generated assume that the sales tax credit will generally be reserved toward the incremental facilities costs needed to accommodate the staff additions required to serve the PAA. An alternative approach might be that, once a balanced scenario is generated, the City can make explicit

decisions on what additional service levels, if any, should be funded by the sales tax credit during the first 10 years.

State Sales Tax Credit Refresher

Council requested a "refresher" on the rules and mechanics of the state sales tax incentive provided for annexations.

Summary of 2006 Legislation

The following excerpt from Senate Bill Report (SB 5321) that amends the original legislation provides a useful recap of the key provisions of **original** legislation:

***"Background:** In 2006 legislation was enacted allowing a city to impose a sales and use tax to provide, maintain, and operate municipal services within a newly annexed area. The tax is a credit against the state sales tax, so it is not an additional tax to a consumer. The tax is for cities that annex an area where the newly received revenues received from the annexed area do not offset the costs of providing services to the area.*

There are several requirements that have to be met before a city may impose the tax. The city must:

- *Have a population less than 400,000;*
- *Be located in a county with a population greater than 600,000;*
- *Annex an area consistent with its comprehensive plan;*
- *Commence annexation of an area having a population of at least 10,000 prior to January 1, 2010; and*
- *Adopt a resolution or ordinance stating that the projected cost to provide municipal services to the annexation area exceeds the projected general revenue the city would otherwise receive from the annexed area on an annual basis.*

The tax rate is 0.1 percent for each annexation area with a population between 10,000 and 20,000 and 0.2 percent for an annexation area over 20,000. The maximum cumulative tax rate a city can impose is 0.2 percent. The tax must be imposed at the beginning of a fiscal year and must continue for no more than ten years from the date it is first imposed. All revenue from the tax must be used to provide, maintain, and operate municipal services for the annexation area. The revenues may not exceed the difference of the amount the city deems necessary to provide services for the annexation area and the general revenue received from the annexation. If the revenues do exceed the amount needed to provide the services, the tax must be suspended for the remainder of the fiscal year. Prior to March 1 of each year, the city must notify the Department of Revenue of the maximum amount of distributions it is allowed to receive for the upcoming fiscal year."

Some additional points of clarification:

- The credit applies to sales taxes collected within the existing city limits and within the boundaries of the annexation area.
- State funding for annexations is available to those cities that have "commenced" the annexation process by January 1, 2010. In this context, "commenced" was determined

by the Department of Revenue to be the point when the Council has passed a resolution declaring its intent to annex. At the request of the City, Representative Larry Springer has agreed to request an Attorney General's (AG) opinion to clarify the term "commence." Based on an "informal" AG letter, staff has assumed that, at a minimum, the City must adopt an annexation resolution and file a certified copy of the resolution with the King County Council to commence annexation. It is important to confirm this interpretation, as the annexation decision will be predicated on qualifying for the state sales tax credit.

- The revenue cannot be used for infrastructure (capital) expenditures. In the most recent financial model, staff assumed that the credit would be used to pay debt service (in the form of a rental charge) on facilities expansions needed to house new staff. The debt would be structured so that the state sales tax would be used first for the annexation area's share of the facilities expansion. In doing so, after ten years, the impact to the operating budget is mitigated.

Phasing of Annexation Under Current Legislation

The 2006 populations of Kirkland's annexation areas are as follows:

Kingsgate	11,700
Juanita	5,600
Finn Hill	15,300

Both the Kingsgate and Finn Hill areas individually meet the 10,000 population threshold for eligibility for the 0.1 percent sales tax credit. In order to be eligible for the 0.2 percent sales tax credit, Kirkland would have to annex both Juanita and Finn Hill, or Kingsgate and Finn Hill or all three annexation sub-areas.

Assuming all three areas are annexed at once, revenue from the state sales tax was initially estimated at \$4.9 million per year beginning in 2010. Updates based on recent sales tax performance were included in the financial model and the sales tax credit figure in the first year of annexation is estimated at \$4.2 million.

Current Legislative Activity

Under SB 5321, the requirement that a city have a population less than 400,000 in order to impose the sales and use tax is eliminated (making Seattle eligible for sales tax credit funds). Any city with a population greater than 400,000 that annexes an area with a population of at least 10,000 may impose the sales and use tax at a rate of 0.0034 percent for each annexed area. The 0.0034 percent rate is also the cumulative rate maximum if a city annexes multiple areas.

The legislation also extends the deadline for qualifying for the sales tax credit, adding a period from January 1, 2011 through January 1, 2021. Consequently, annexations that commence before January 1, 2010 would still be eligible for funding under the current law. If the January 2010 date was not met, then a new funding cycle would not be available until 2011. This bill provides for an extension but recognizes the current budget difficulties faced by the state and moves the sales tax credit out of the coming biennium to the next.

A question has been raised based on the draft language in the following section (emphasis added):

*(5) The tax imposed by this section shall only be imposed at the beginning of a fiscal year and shall continue for no more than ten years from the date that **each increment** of the tax is first imposed. Tax rate increases due to additional annexed areas shall be effective on July 1st of the fiscal year following the fiscal year in which the annexation occurred, provided that notice is given to the department as set forth in subsection (((8))) (9) of this section.*

The question is whether this would allow a City annexing over 20,000 to impose the sales tax increments at two 0.1% increments at two different points in time, for example, the first 0.1 percent from 2010-2020 and the second 0.1% from 2013-2023 to better match how costs would be incurred. One of the drafters of the bill has indicated that the language was intended to address a situation where two annexations between 10,000 and 20,000 occur at two different points in time, allowing them to qualify for a total of .2% sales tax credit during the period of overlap. It is unclear if the first circumstance would also qualify. We should have a better idea of whether this bill will survive by the March 3 Study Session, as it needs to pass out of the originating committee by February 25.

Sales Tax Credit Mechanics

The 10-year state sales tax credit is an integral part of the annexation financial analysis. The State has not issued formal guidance as to how the state sales tax credit will be administered and what specific documentation will be required to demonstrate shortfalls, however, meetings have been initiated with the State Auditor's Office to discuss the issue. At this stage, we are monitoring the experiences of Auburn and Renton, who had annexations that qualify for the credit and will be subject to audit of the sales tax credit for 2008. Auburn's experience to date has provided two insights: (1) that detailed record-keeping will be necessary to demonstrate qualifying costs, and (2) that timing is critical to maximize the credit. We will continue to stay in contact with both jurisdictions, and others considering this option, to track their "lessons learned".

Refresher on Validation

Below is an excerpt from the King County Elections website describing validation requirements. This relates to annexation because the City is planning to place the question of assuming the City's voted indebtedness on the ballot with the annexation question, triggering the bond validation requirement.

"Passing a levy or bond issue isn't always a simple matter of majority rules. State law makes bond issues and some types of levies tougher to pass by requiring a "super majority. Other levies such as levy lid lifts and levies for schools only require a simple majority.

State Constitution (Article 7 Section 2) mandates the validation requirements for excess levies and bond issues.

Levy Validation (excluding school levies)

To validate, levies must pass with a 60% favorable majority. They must also win a minimum number of YES votes based on the number of people who voted in the previous November General Election within the school or fire, etc., district. That minimum number of YES votes is determined by taking 60% of 40% of the people who voted in the most recent General Election.

Example: If there were 10,000 votes cast in the last General Election:

10,000

x 40%

4,000

x 60%

2,400= Minimum number of "yes" votes required to validate.

To pass the levy, the district needs to have at least 2,400 YES votes, even if only a total of 2,500 people vote on the levy.

Levy Validation for Schools

To validate a school levy, a simple majority is required.

Bond Validation

Bond issues must validate two ways. They must pass with a 60% favorable majority, or 60% of ballots cast are "Yes" votes. In addition, they have a voter turnout requirement that levies don't have. The turnout must equal 40% of the voters who cast ballots in the last General Election. So, a bond measure could get the required number of YES votes, but could still fail if not enough people vote in the election.

Example: 10,000 people voted in the XYZ School District in last year's November General Election.

To pass this bond issue, the XYZ District must also ensure that at least 4,000 people vote in the bond election. Of those, at least 2,400 must vote YES."

An evaluation of the 2003-2006 election returns from the PAA completed in 2006 indicates that the voting patterns in the annexation area are very similar to voting patterns of the current residents of Kirkland. Annexation area vote results were generally within one to two percentage points of the City of Kirkland results. In the absence of PAA specific validation data (the area falls within 3 voting districts making it difficult to extract specific statistics), an estimate based on the City's validation statistics is provided in the following table.

2008 Validation Statistics

City of Kirkland population	48,410	PAA Population (Note 1)	33,016
Active Registered voters (.61028%)	29,544	Active Registered voters (.61028%)	20,149
Total votes cast 11/04/08 (84%)	24,790	Total votes cast 11/04/08 (84%)	16,925
40% of votes cast minimum to validate (40%)	9,916	40% of votes cast minimum to validate (40%)	6,770
60% of 40% minimum yes votes required (60%)	5,950	60% of 40% minimum yes votes required (60%)	4,062

Note 1: Assuming growth is consistent with the City of Kirkland average growth rate of 101.1%, the 2008 population in the PAA is estimated at 33,016.

Under the assumption of similar voting patterns in the PAA, there would need to be 6,770 votes cast in 2009 to validate, this is 40% of the estimated number of votes cast in the 2008 election. Of these 6,770 votes required for validation purposes, 60% (or approximately 4,062 of the 6,770) would need to vote yes to actually pass annexation. Validation is only required if the annexation ballot includes a "yes" or "no" vote on whether annexation area residents are willing to share in the City's bonded indebtedness.

City of Bothell Study of Kirkland's PAA

In 2008, the City of Bothell commissioned a study at the urging of King County regarding the feasibility of Bothell's annexation of Kirkland's PAA. King County's request came after the Kirkland City Council deferred a decision on annexation until after the 2009/2010 Budget was completed. The City of Bothell contracted with Nesbitt Planning and Management Inc. to conduct a financial feasibility study for extending city operations to Kirkland's potential annexation area (PAA). Bothell staff presented the report to their City Council at a study session on January 13 and held a follow-up study session on February 10. Following is a high-level summary comparing Bothell's financial analysis to Kirkland's analysis of the same area.

Study Scope and Methodology

The Nesbitt study utilized a methodology similar to the one used by Randy Young and Associates when they completed the 2002 Kirkland annexation study. The methodology essentially uses the City budget as a base, identifies fixed versus variable costs, and then uses "cost drivers" to extrapolate the marginal cost of serving the annexation area. Cost drivers are factors such as population, calls for service and permits issued. Subsequent Kirkland studies used a more direct approach with departments preparing annexation budgets. Both approaches resulted in a deficit position for annexation for Kirkland.

The Nesbitt study relied heavily on data produced for Kirkland's most recent annexation study completed in 2007-2008. The Nesbitt study did not include a detailed analysis of capital needs in the annexation area and did not include an analysis of additional facilities' costs needed to house new staff.

Kirkland's study included a twenty year forecast for existing Kirkland, the PAA and the combined larger city in order to understand the relative growth patterns for each area alone and together.

This approach was used to address the question of whether the annexation would have a long term positive or negative impact on the existing city's financial position.

The difference in the forecast horizon is one of the most striking differences between the scope of the two studies. Kirkland's study projected annexation costs and revenues out twenty years in order to fully understand the long term potential impact of the loss of the state sales tax subsidy after ten years. The Kirkland Council specifically asked for a "steady state" analysis. The Nesbitt study extended the analysis out for four years. In the fourth year, the one-time capital equipment costs were amortized which resulted in a neutral financial outcome assuming continued receipt of the state sales tax. As a reminder, a city is only be eligible for the state sales tax to the extent that a deficit can be demonstrated (i.e. the deficit amount is the maximum amount of state sales tax available per year). If the analysis were extended out past ten years, it appears as though Bothell would have a negative financial position similar to that shown by Kirkland's analysis.

Revenue and Expenditure Assumptions

Bothell's revenue estimates were calculated using similar assumptions as those used for Kirkland's study for items such as property tax, utility tax and sales tax. Aside from fundamental differences in the two cities' existing tax structures, a few differences were noted:

- Bothell assumed gambling tax revenue would be available using the 11 percent tax rate currently imposed by King County (\$580,000 based on the 2006 King County receipts).
- The Toyota dealership planning to relocate from incorporated to unincorporated King County is included in the Bothell analysis as contingent revenue (\$350,000 for 2009).

The Nesbitt report projects expenditures by taking the 2009 adopted budget for Bothell and extending it based on selected "drivers." A total of just under one hundred new FTE's resulted from the Nesbitt analysis methodology. City of Bothell staff disagreed with the consultant's staffing level and recommended additional police and fire personnel based on their own estimate of staff needed to serve the area at Bothell's level of service. An additional 13.74 FTE's and related costs were recommended by Bothell Police and Fire for an added expense of \$2.3 million for 2009.

A direct comparison of Bothell and Kirkland annexation staffing levels would be difficult given the different service systems provided by the two cities and differences in organizational structure. For instance, fewer overall police staff is recommended, however, Bothell currently has a higher ratio of police personnel per capita than Kirkland, so the base is different. Likewise, Bothell's deployment of fire and emergency medical personnel takes into account the location of existing fire stations in addition to stations that would transfer to Bothell from Fire District #41. Also, Kirkland's Fire department includes building staff and it is not clear where these staff are in the Bothell study without further analysis and discussion with Bothell staff. The following table summarizes estimated staffing reflected in the both cities' annexation analysis.

	Bothell	Kirkland	Difference
Judicial	2.95	6.70	3.75
Executive	1.97	1.00	(0.97)
Finance/City Clerk	3.14	4.00	0.86
Legal	1.40	1.50	0.10
Human Resources	1.50	1.80	0.30
Facilities	0.98	1.25	0.27
Information Services	2.25	7.50	5.25
Police	47.89	52.50	5.25
Fire/Building*	26.50	19.00	(7.50)
Public Works**	9.00	15.50	6.50
Parks	8.39	10.45	2.06
Community Development	6.75	9.00	2.25
Total	112.72	130.20	18.12

*Includes addition of engine company to Kirkland Fire for area currently served by Woodinville Fire and Life Safety

**Kirkland Public Works FTE excludes CIP project engineers that would be funded from the CIP

As noted earlier, the other major difference between Kirkland and Bothell's expenditure estimates lies in assumptions about facility costs. Kirkland's study included debt service for facilities needed to house new staff. Bothell's study does not yet take into consideration marginal facilities costs that should be attributed to the annexation area.

The table that follows summarizes Bothell's financial analysis before factoring in the state sales tax incentive funding (estimated at \$3.1 million for 2009).

Unrestricted Operating Revenue	14,238,000
Toyota Dealership	350,000
Card Room	580,000
Subtotal Revenue	15,168,000
Nesbitt Report Estimated Expenditures	14,613,000
Fire and Police Recommended FTE Adds	2,252,359
Subtotal Operating Expenditures	16,865,659
Net Operating Costs	(1,697,659)

The most comparable figure for Kirkland would be the last estimate provided in April 2008 that reflected the baseline analysis with the alternative service delivery model, since that version reflects assumption similar to those used by Bothell. At that time, Kirkland's projected net cost in the annexation area resulted in a deficit of about \$405,000 for 2010 excluding facilities costs and the state sales tax incentive. Kirkland's "bottom line" after considering facilities costs and the state sales tax resulted in a 2010 deficit amount of \$1.554 million. If Kirkland assumed

gambling tax revenue were available at the King County tax rate of 11% as assumed by Bothell, that deficit would be reduced to just under \$1 million. With the revenue changes in the 2009 update under the 3-District scenario, the deficit would fall even further.

At the January 13 meeting the Bothell City Council directed staff to return with additional analysis and information:

- Estimated capital needs and costs,
- Clarification regarding the term "commence" in the state sales tax incentive legislation,
- An analysis of the differing staffing levels recommended for the north Bothell annexation compared to the south Bothell – the "SOBA" (Bothell is also considering annexation of an area to the north – the "NEWBA"),
- Information regarding potential county financial support (King and Snohomish),
- Comparison of density of the two annexation areas including commercial development potential,
- Kirkland's timetable for deciding whether to retain or relinquish its Potential Annexation Area,
- Discussion of NEWBA versus SOBA pros and cons.

At their February 10 study session, the City Council received updated information (see Attachment F for the Bothell staff report). During the study session, Mayor Lamb clarified Bothell's position relative to Kirkland's intentions:

- Bothell understands that they cannot begin annexation proceedings of Kirkland's PAA without action on Kirkland's part to relinquish the area. Bothell is not interested in working counter to Kirkland's wishes.
- Bothell will suspend significant additional staff work on analyzing the SOBA until the Kirkland City Council holds its March 3 meeting and indicates whether they intend to pursue the annexation or relinquish the area. Mayor Lamb noted that Kirkland has studied the potential annexation for five years and so he did not anticipate definitive direction on March 3.
- Bothell will perform additional study on the feasibility and time frame for annexing all of Bothell's assigned annexation areas in Snohomish and King Counties.

At both meetings, the Bothell City Manager concluded that both the north and south annexations were "financially feasible" although the north annexation showed a better financial outcome than the SOBA. Presumably, they would achieve a uniform level of service across the entire City over time and believe that the amount of the deficit is manageable (i.e. they could still provide an acceptable level of service in the annexed areas).

If Bothell were to annex Kirkland's PAA, there would be significant impacts to the City of Kirkland budget because Bothell would take over the area served by King County Fire District #41 (FD 41), which is currently served under contract by the City of Kirkland. Without the FD 41 service area, the location and staffing of fire stations would need to be re-evaluated. A detailed analysis of these impacts would need to be conducted if this option is pursued.

Gambling Legislation Update

The annexation financial model assumed that the casino currently located in the Kingsgate area would close based on Kirkland's prohibition on house-banked card rooms. Current land use law requires an "all or nothing" approach to card rooms. Card rooms are either prohibited throughout the City or must be allowed in any area of the City (consistent with other zoning regulations limiting their location). In their legislative agenda, the City Council indicated support for legislation that would allow existing casinos in annexation areas to be "grandfathered" in (i.e. allowed to continue to operate) without having to allow additional card rooms throughout the city.

HB 2162 was introduced on February 11th and referred to the Commerce and Labor Committee. The Commerce and Labor Committee passed the Substitute House Bill out of committee on February 20th. The bill allows for local control of gambling establishments and specifically allows a city that annexes an area where gambling establishments are allowed and currently licensed to continue to allow the establishment to operate without having to allow additional casinos. The legislation would allow the Kirkland City Council to decide whether to immediately extend its ban on card rooms to the annexation area or allow the existing casino to continue to operate. If gambling is prohibited in the newly annexed area, the City could not impose its ban on the existing casino for at least three years.

Summary and Options for Next Steps

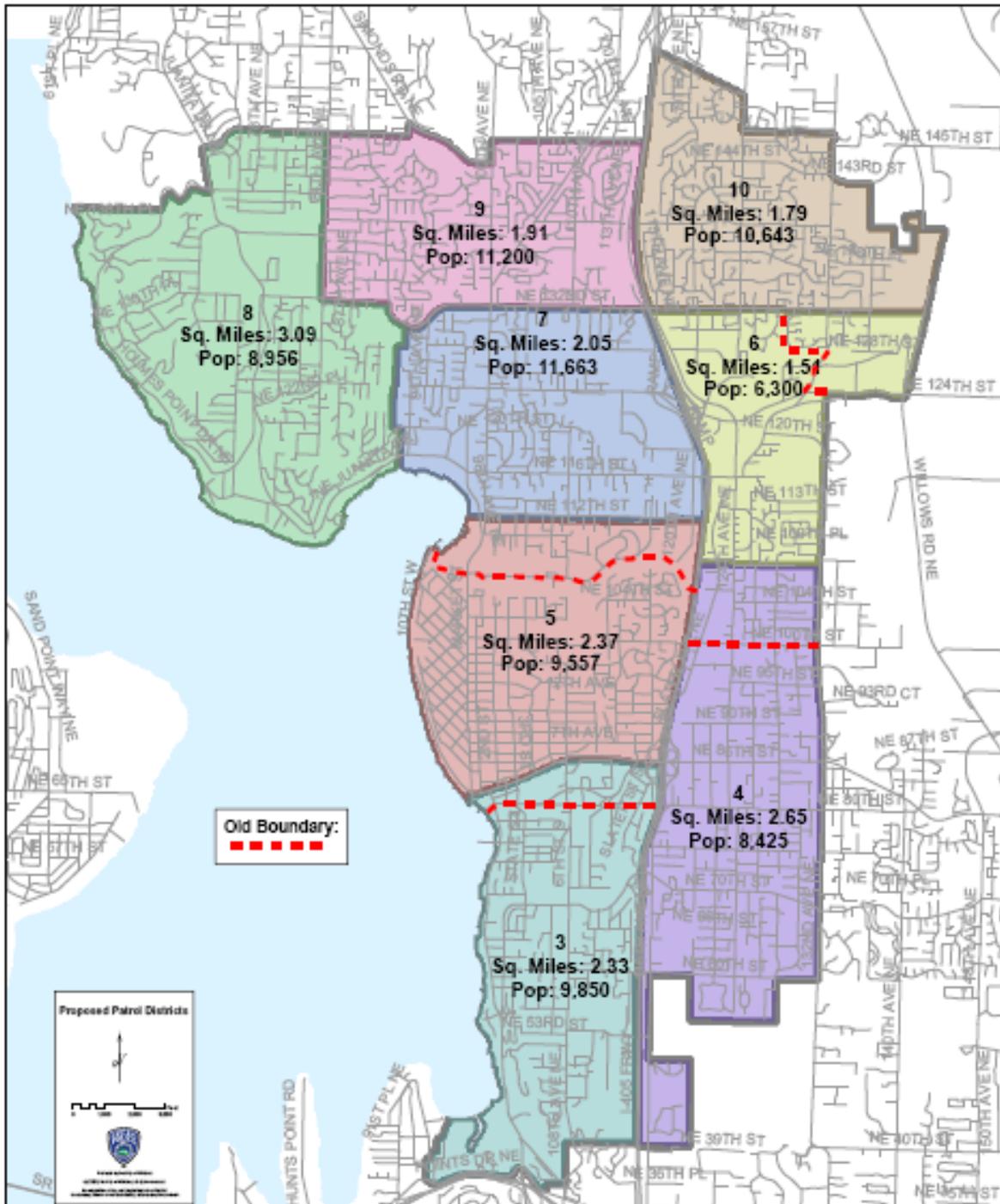
The results of this update reflect that there were positive impacts for annexation resulting from the Council's actions to balance the 2009-2010 budget and create a more sustainable revenue stream by decreasing reliance on sales tax and increasing reliance on utility taxes (assuming passage of the private utility tax increase). In addition, the recognition that initial service levels may vary in the PAA, as represented by the Alternate Service Delivery model, also helps produce a workable scenario. The contingency related to locating the required public safety facilities on the City Hall campus, rather than in a separate facility, also improves the annexation scenarios.

There are three potential options for next steps:

1. Direct staff to proceed with the Boundary Review Board process and bring back information on recommended election dates.
2. Discontinue the evaluation process and determine whether the City would consider relinquishing the PAA to Bothell.
3. Identify additional follow up information required to make a decision and outline a process and timeline for making that decision. Note that, if annexation is likely to occur at some point in time, qualifying to receive the state sales tax credit is a significant benefit toward easing the transition process. Given the current interpretation of "commence" and existing terms of the legislation, a resolution calling for the election would need to be passed before December 31, 2009.

If the decision is made to proceed with annexation, a detailed cash flow analysis will be developed to determine the optimal effective date from a revenue perspective, as well as a plan for funding the transition needs in advance of that date.

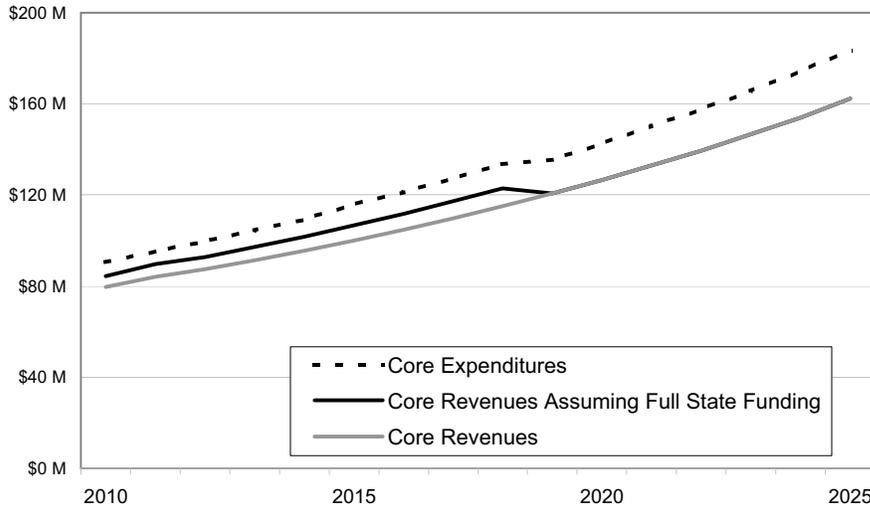
Proposed Patrol Districts



Scenario: Phase-II Baseline With Annexation & Alternative Service Delivery (ASD)

Tax Policies	Expenditure Management Policies	Development
No change in tax policy 1% property tax limit	Hiring rate reflects current policies Alternative Service Delivery (ASD) & 3 Police districts in PAA	Baseline

Plus Additional Costs



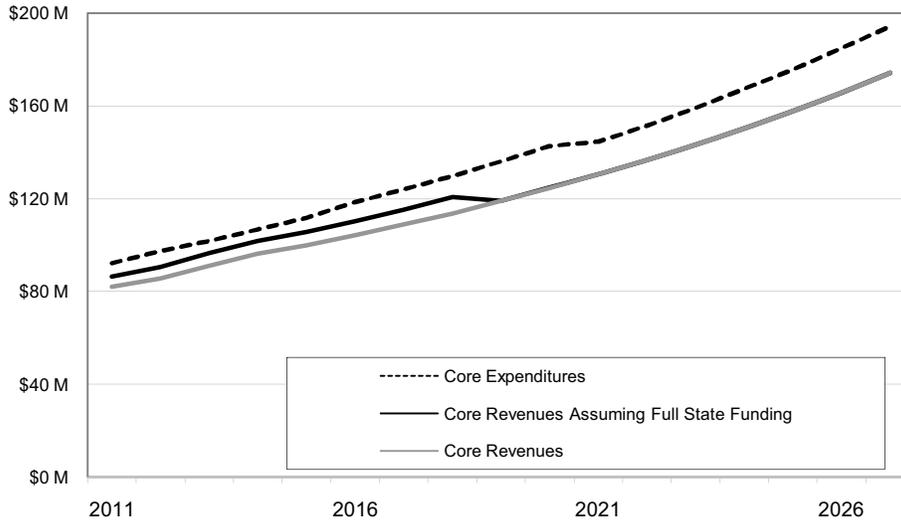
Current Kirkland	2010	2015	2020	2025
Core Expenditures (000's)	64,906	83,567	107,443	138,110
Facility Debt Service (000's)	2,295	2,303	2,288	2,254
Subtotal Expenditures	67,201	85,869	109,731	140,365
Core Resources (000's)	62,741	78,551	97,907	122,627
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	62,741	78,551	97,907	122,627
Net Resources (000's)	(4,460)	(7,318)	(11,824)	(17,738)
Deficit as % of Expenditures	-7%	-9%	-11%	-13%

Increment from PAAs	2010	2015	2020	2025
Core Expenditures (000's)	17,149	24,053	31,821	42,240
Facility Debt Service (000's)	6,078	6,070	993	1,027
Subtotal Expenditures	23,227	30,123	32,814	43,267
Core Resources (000's)	16,744	21,516	28,638	39,543
State Sales Tax Credit ('000's)	4,929	6,527	0	0
Subtotal Revenues	21,673	28,043	28,638	39,543
Net Resources (000's)	(1,554)	(2,080)	(4,175)	(3,724)
Deficit as % of Expenditures	-9%	-9%	-13%	-9%

Entire City	2010	2015	2020	2025
Core Expenditures (000's)	82,056	107,620	139,264	180,351
Facility Debt Service (000's)	8,373	8,373	3,281	3,281
Subtotal Expenditures	90,428	115,992	142,545	183,632
Core Resources (000's)	79,485	100,068	126,545	162,170
State Sales Tax Credit ('000's)	4,929	6,527	0	0
Subtotal Revenues	84,414	106,594	126,545	162,170
Net Resources (000's)	(6,014)	(9,398)	(15,999)	(21,462)
Deficit as % of Core Expenditures	-7%	-9%	-11%	-12%

FEBRUARY 2009 SCENARIOS

**3-District, 7.5% Private Utility Tax
Annexation in 2010**



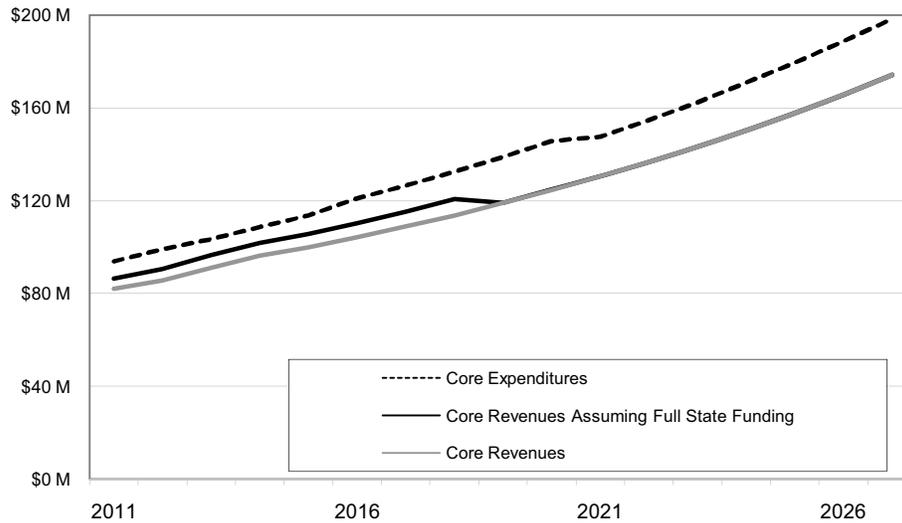
Current Kirkland	2011	2016	2021	2026
Core Expenditures (000's)	66,557	86,486	110,911	142,603
Facility Debt Service (000's)	2,577	2,586	2,575	2,551
Subtotal Expenditures	69,134	89,072	113,486	145,153
Core Resources (000's)	64,765	82,156	101,551	127,150
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	64,765	82,156	101,551	127,150
Net Resources (000's)	(4,369)	(6,916)	(11,936)	(18,003)
Deficit as % of Expenditures	-7%	-8%	-11%	-13%

Increment from PAAs	2011	2016	2021	2026
Core Expenditures (000's)	16,786	23,096	29,959	38,457
Facility Debt Service (000's)	6,379	6,370	1,075	1,099
Subtotal Expenditures	23,164	29,466	31,033	39,556
Core Resources (000's)	17,315	22,028	28,986	38,698
State Sales Tax Credit ('000's)	4,240	6,055	0	0
Subtotal Revenues	21,555	28,083	28,986	38,698
Net Resources (000's)	(1,609)	(1,383)	(2,048)	(858)
Deficit as % of Expenditures	-10%	-6%	-7%	-2%

Entire City	2011	2016	2021	2026
Core Expenditures (000's)	83,343	109,582	140,870	181,059
Facility Debt Service (000's)	8,956	8,956	3,650	3,650
Subtotal Expenditures	92,298	118,538	144,520	184,709
Core Resources (000's)	82,081	104,183	130,537	165,848
State Sales Tax Credit ('000's)	4,240	6,055	0	0
Subtotal Revenues	86,320	110,238	130,537	165,848
Net Resources (000's)	(5,978)	(8,299)	(13,983)	(18,861)
Deficit as % of Core Expenditures	-7%	-8%	-10%	-10%

FEBRUARY 2009 SCENARIOS

4-District, 7.5% Private Utility Tax
Annexation in 2010



Current Kirkland	2011	2016	2021	2026
Core Expenditures (000's)	66,554	86,482	110,907	142,597
Facility Debt Service (000's)	2,577	2,586	2,575	2,551
Subtotal Expenditures	69,130	89,068	113,481	145,147
Core Resources (000's)	64,765	82,156	101,551	127,150
State Sales Tax Credit ('000's)	0	0	0	0
Subtotal Revenues	64,765	82,156	101,551	127,150
Net Resources (000's)	(4,365)	(6,912)	(11,931)	(17,997)
Deficit as % of Expenditures	-7%	-8%	-11%	-13%

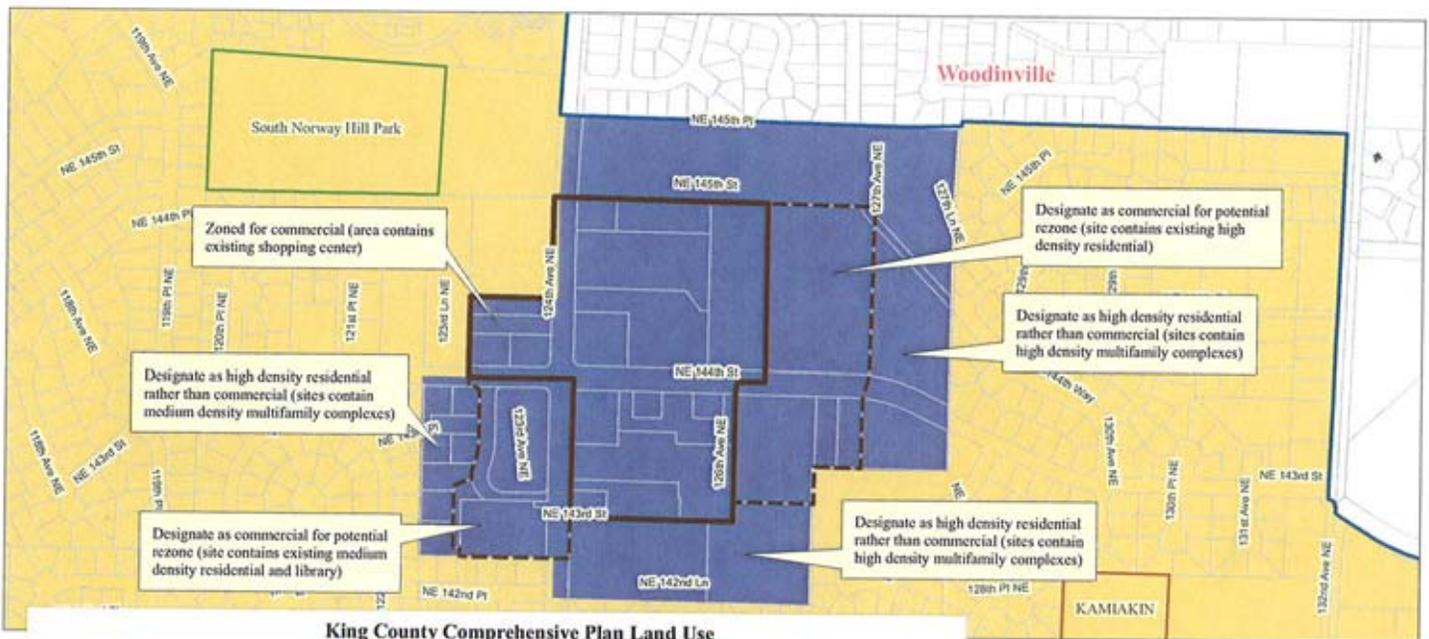
Increment from PAAs	2011	2016	2021	2026
Core Expenditures (000's)	18,304	25,554	33,094	42,462
Facility Debt Service (000's)	6,379	6,370	1,075	1,099
Subtotal Expenditures	24,683	31,924	34,169	43,562
Core Resources (000's)	17,315	22,028	28,986	38,698
State Sales Tax Credit ('000's)	4,240	6,055	0	0
Subtotal Revenues	21,555	28,083	28,986	38,698
Net Resources (000's)	(3,128)	(3,841)	(5,183)	(4,864)
Deficit as % of Expenditures	-17%	-15%	-16%	-11%

Entire City	2011	2016	2021	2026
Core Expenditures (000's)	84,858	112,036	144,001	185,059
Facility Debt Service (000's)	8,956	8,956	3,650	3,650
Subtotal Expenditures	93,814	120,992	147,651	188,709
Core Resources (000's)	82,081	104,183	130,537	165,848
State Sales Tax Credit ('000's)	4,240	6,055	0	0
Subtotal Revenues	86,320	110,238	130,537	165,848
Net Resources (000's)	(7,494)	(10,753)	(17,114)	(22,861)
Deficit as % of Core Expenditures	-9%	-10%	-12%	-12%

KINGSGATE COMMERCIAL CENTER

EXISTING COMP PLAN

Kingsgate Commercial Business Center Proposed Changes To King County Comprehensive Plan Land Use Map



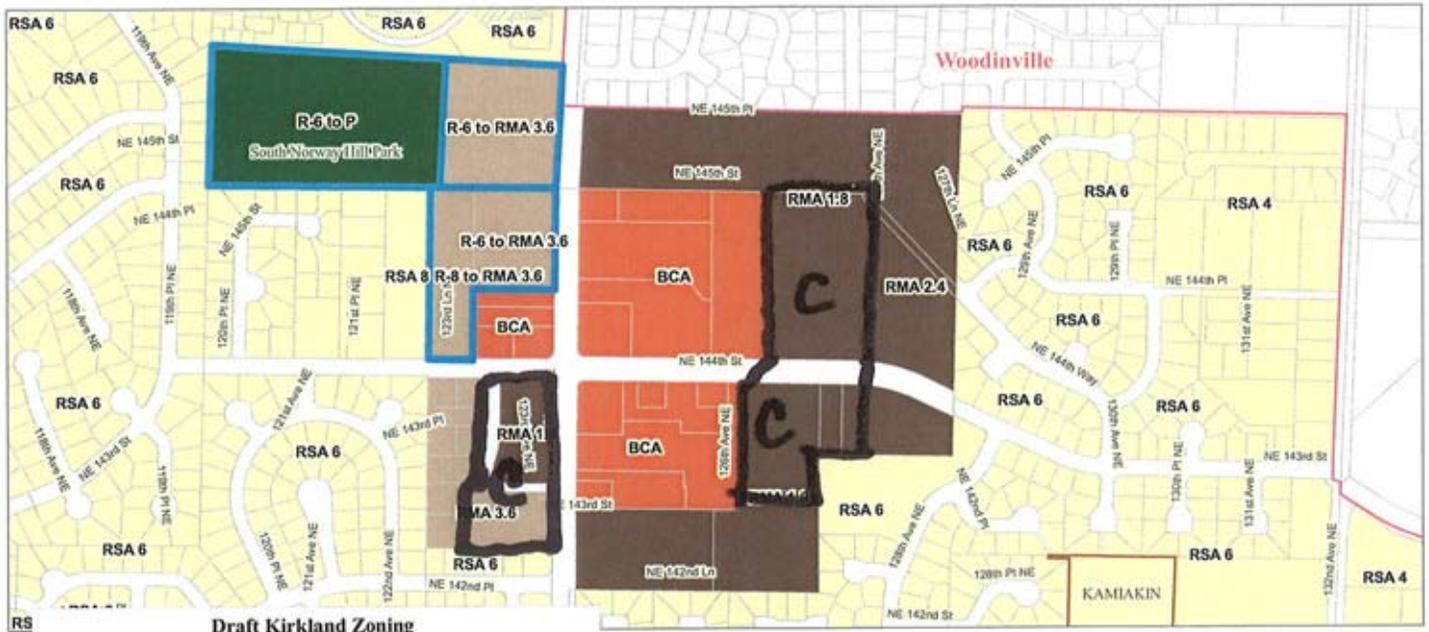
King County Comprehensive Plan Land Use

	Community Business Center		Urban Residential, High, >12 du/ac		Greenbelt / Urban separator
	Neighborhood Business Center		Urban Residential, medium, 4-12 du/ac		
	Commercial Outside of Centers		Industrial		

KINGSGATE COMMERCIAL CENTER



2/19/08 COUNCIL MEETING



= Designate commercial

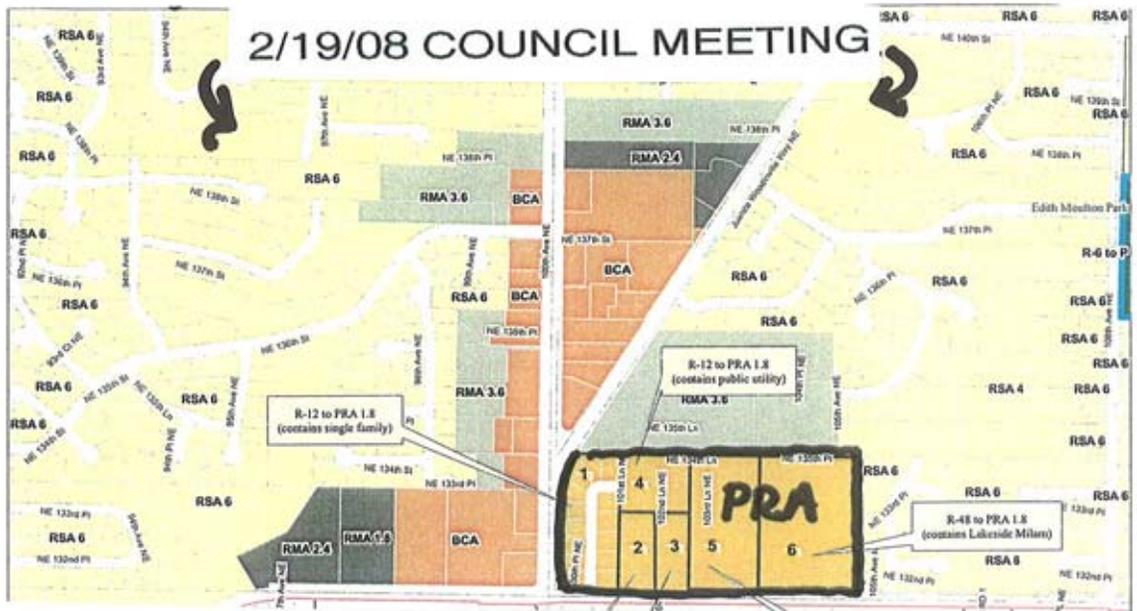


4/8/08 COUNCIL ANNEXATION COMMITTEE



= Designate commercial

JUANITA COMMERCIAL CENTER

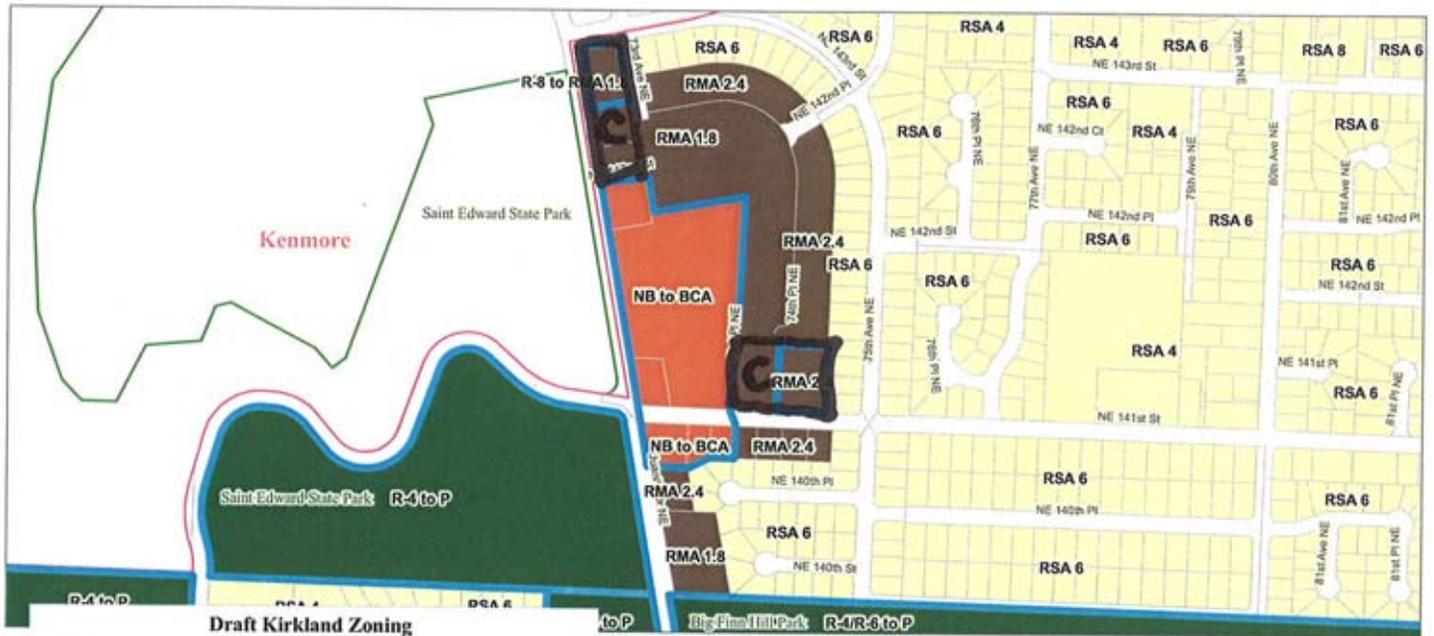


Note: Numbers in office area (orange) correspond to table in the staff memo

= Designate Commercial = Designate Professional Office/Residential

NORTH FINN HILL COMMERCIAL CENTER

2/19/08 COUNCIL MEETING



= Designate commercial

4/8/08 COUNCIL ANNEXATION COMMITTEE

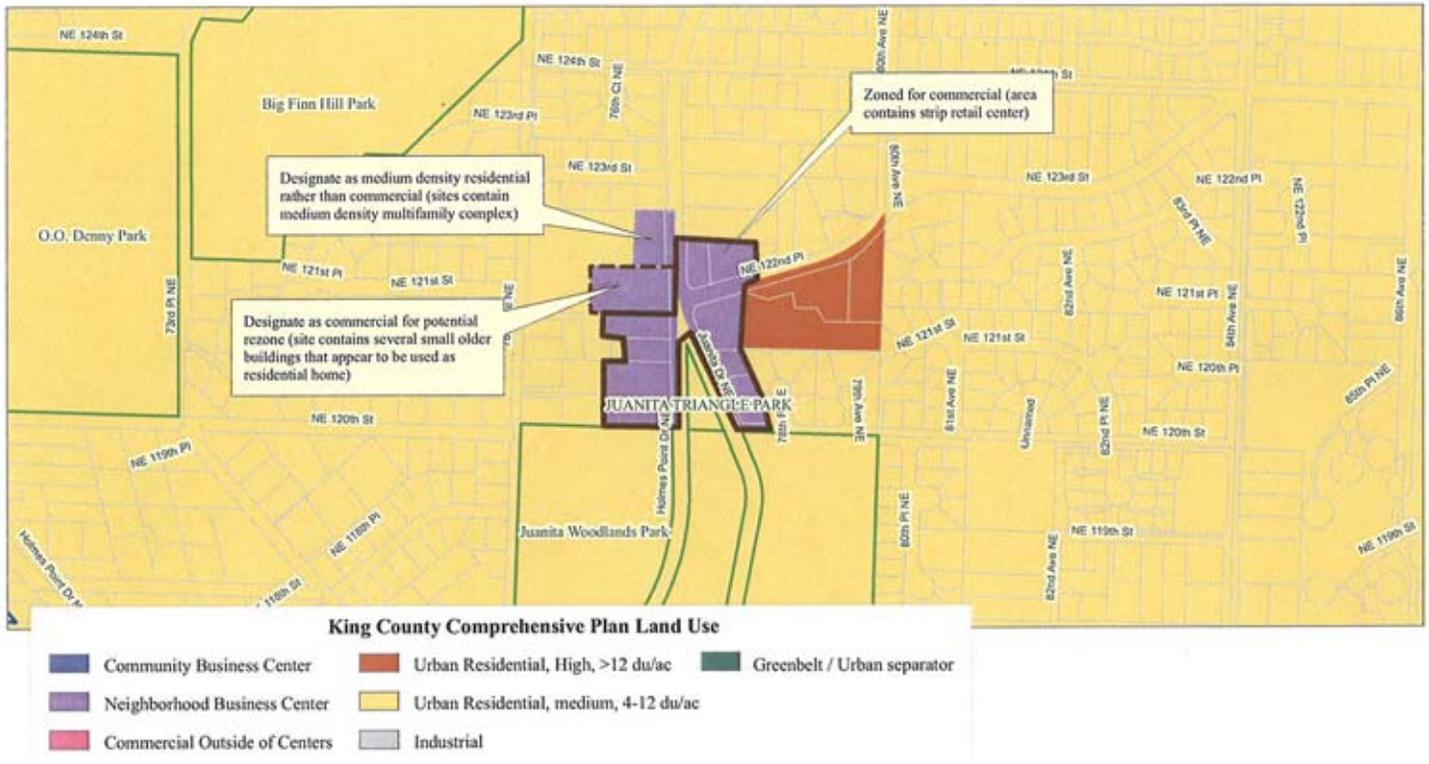


= Designate commercial

SOUTH FINN HILL COMMERCIAL CENTER

EXISTING COMP PLAN

South Finn Hill Neighborhood Business Center Proposed Changes To King County Comprehensive Plan Land Use Map



SOUTH FINN HILL COMMERCIAL CENTER

2/19/08 COUNCIL MEETING

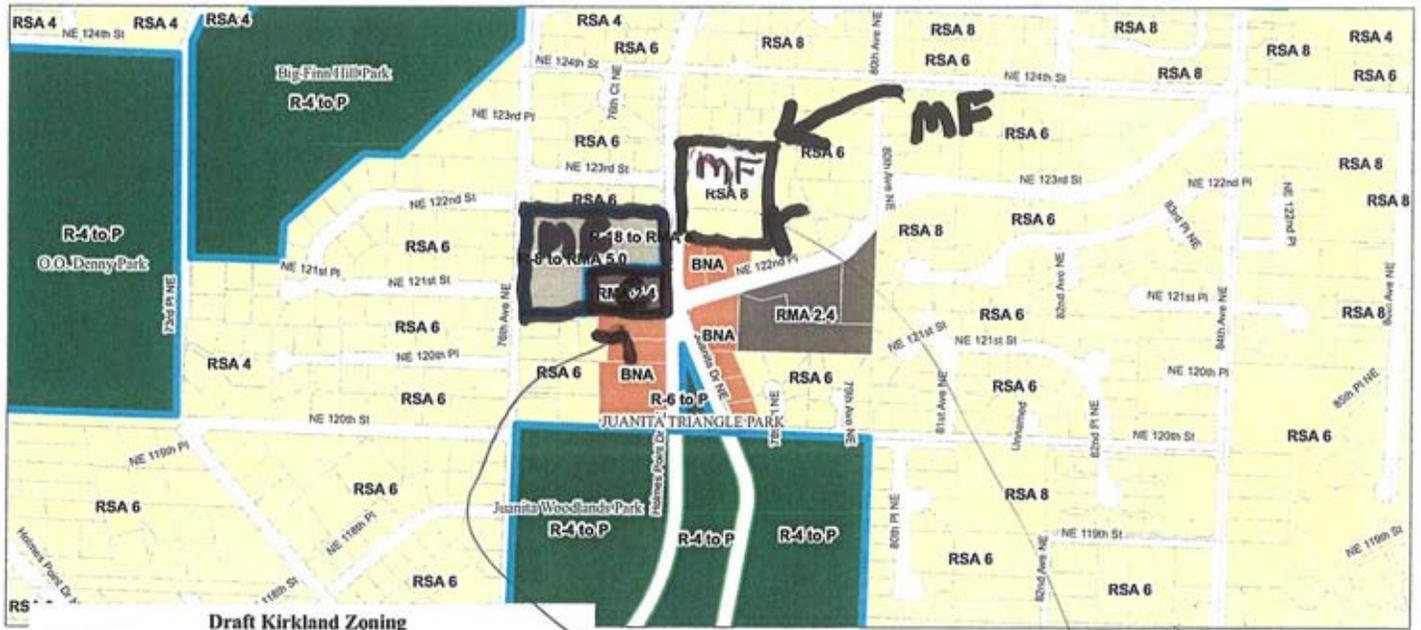


Draft Kirkland Zoning

- Commercial
- Medium Density Residential
- Office
- Low Density Residential
- High Density Residential
- Park/Open Space

C = Designate commercial
Rm = Designate multifamily

4/8/08 COUNCIL ANNEXATION COMMITTEE

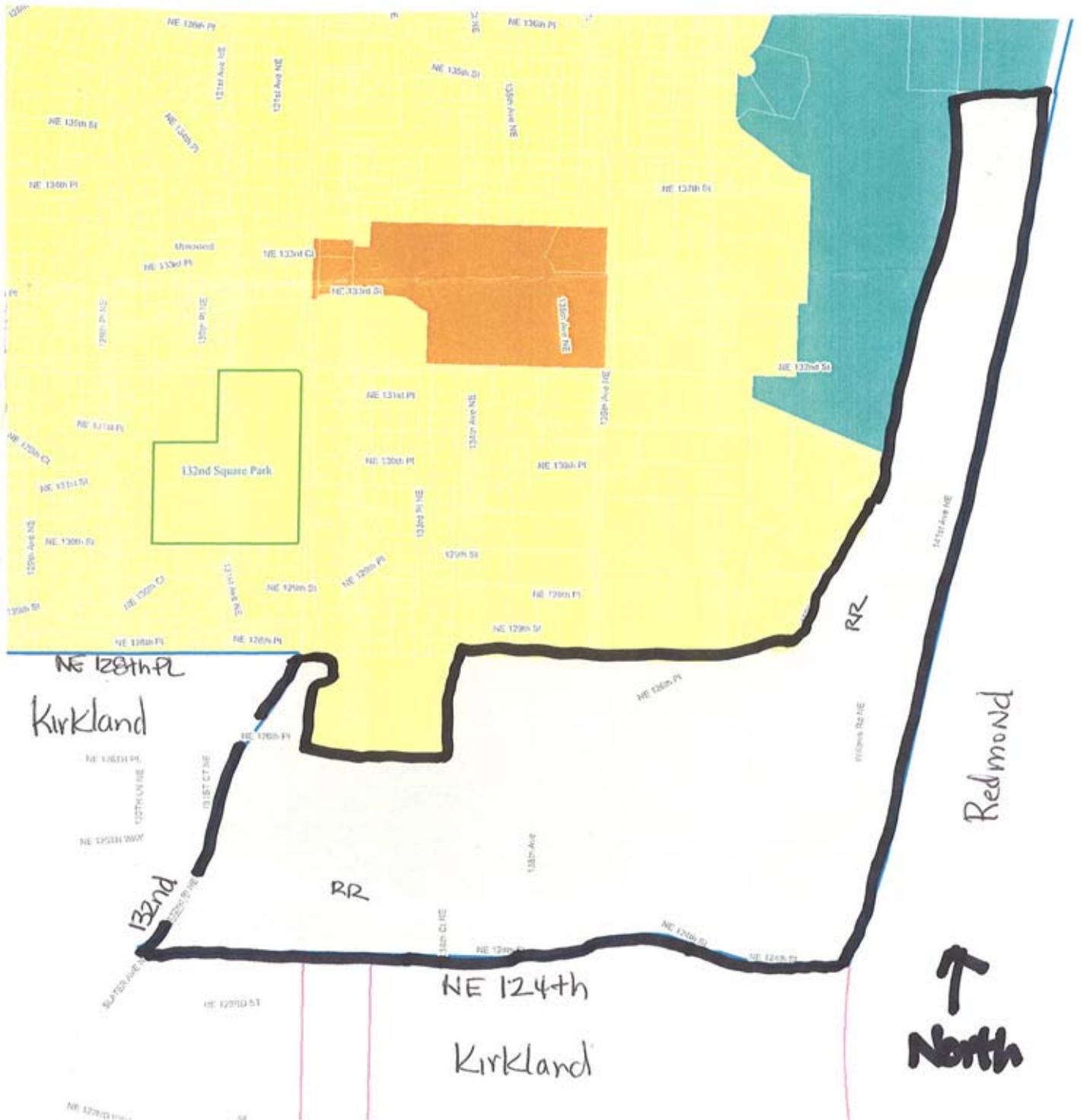


Draft Kirkland Zoning

- Commercial
- Medium Density Residential
- Office
- Low Density Residential
- High Density Residential
- Park/Open Space

C = Designate Commercial
MF = Designate multifamily

TOTEM LAKE INDUSTRIAL AREA



Bothell City Council
AGENDA BILL SUMMARY

Meeting Date: 10 Feb 2009
Type: Study Session Item
Subject: **Continued Study Session to Consider Potential South of Bothell Annexation (SOBA)**
Budget Impact and Source of Funds: Work on the potential South of Bothell Annexation has been programmed and funded in the 2009-10 budget.
Contact Person / Department: Steve Anderson, Deputy City Manager / Executive Department

EXECUTIVE SUMMARY:

This Study Session provides for continued Council discussion from its January 13 meeting regarding the potential South of Bothell Annexation (SOBA). To assist Council, a staff report (see Attachment 1) has been prepared which includes the following:

- Responses to questions raised by Council at its January 13 Study Session;
- An explanation of the revised revenue / expenditure spreadsheet distributed to Council on January 20;
- An update on the NEWBA annexation; and
- A discussion of an alternative annexation scenario in which annexation of Bothell's existing PAA would be pursued concurrent with the NEWBA.

COUNCIL PROCESS:

Study Session

- Presentation by Steve Anderson, Deputy City Manager
- Council discussion: no action necessary

HISTORY:

- July 15, 2008: City Council approves Resolution 1225 (2008) expressing interest in annexation of the Finn Hill, Upper Juanita and Kingsgate areas.
- January 13, 2009: Council conducts Study Session regarding the SOBA.

RECOMMENDED ACTION:

This item is a Study Session: no action is necessary at this time.

ATTACHMENTS:

1. Staff report
 2. Letter dated January 29, 2009, from City Manager Stowe to Snohomish County Executive Reardon
 3. Spreadsheets projecting revenues and expenditures out 12 years based on 3-year and 10-year amortization schedules (previously distributed on January 13, 2009)
 4. Map depicting adopted Bothell MUGA and PAA, and Finn Hill, Upper Juanita and Kingsgate unincorporated areas within Kirkland's PAA
-

Approved by Robert S. Stowe, City Manager, on February 4, 2009

Bothell City Council
AGENDA STAFF REPORT
Attachment 1 to AB

Subject: Continued Study Session to Consider Potential South of Bothell Annexation (SOBA)

Meeting Date: February 10, 2009

Staff Contact: Steve Anderson, Deputy City Manager

This staff report consists of four parts:

1. Responses to questions raised by Council at its January 13, 2009, Study Session
2. An explanation of the revised revenue / expenditure spreadsheet distributed to Council on January 20, 2009;
3. An update on the NEWBA annexation; and
4. A discussion of an alternative annexation scenario in which annexation of Bothell's existing PAA would be pursued concurrently with the NEWBA.

Responses to questions raised by Council at its January 13, 2009, Study Session

1. **How does the SOBA compare with the NEWBA in development and redevelopment potential?**

Staff has requested from King County and Snohomish County data from each county's Buildable Lands reports which would provide some quantifiable indication of the development and redevelopment potential within the SOBA and the NEWBA.

In the meantime, some preliminary observations can be derived from population densities, aerial photos and windshield surveys of the two areas.

The NEWBA totals 3,602 acres and contains an estimated population of 21,980, for an average density of 6.1 persons per acre.

The SOBA (comprising unincorporated South Norway Hill and Brickyard within Bothell's adopted PAA plus unincorporated Finn Hill, Upper Juanita and Kingsgate currently within Kirkland's PAA) totals 5,138 acres and contains an estimated population of 36,056, for an average density of 7.02 persons per acre.

Both the NEWBA and the SOBA are substantially more dense in terms of population than the area within the current Bothell city limits. The existing Bothell corporate boundaries total 7,735 acres and contain an estimated population of 32,860, for an average density of 4.25 persons per acre.

The disparity in density between the City and the two potential annexation areas can be misleading. It does not mean that the residential areas in the NEWBA and the SOBA are

Agenda Staff Report
Subject: Continued Study Session to Consider Potential South of Bothell Annexation (SOBA)
Meeting Date: February 10, 2009
Staff Contact: Steve Anderson, Deputy City Manager

fundamentally different from those in Bothell in terms of character and intensity of development.

Rather, the difference in density is largely explained by the fact that Bothell has two employment centers - in the North Creek and Canyon Park business parks - which are geographically very large and contain few dwelling units. There are no comparable areas in either the NEWBA or the SOBA.

From analysis of recent aerial photos and windshield surveys, the .9-person-per-acre difference between the NEWBA and the SOBA is likely attributable to a slightly lower level of development within the NEWBA. Taking into account the development potential in the many already-approved subdivisions within the NEWBA which are currently lying fallow and in land in the NEWBA likely to be subdivided once the housing sector recovers, the density gap between the NEWBA and the SOBA will probably disappear over the next several years.

As to redevelopment potential, this is an attribute more relevant to commercial areas than to residential areas, since single family and multi-family housing is rarely razed and redeveloped to any substantial degree.

The commercially-zoned areas in both the NEWBA and the SOBA are nearly fully developed, although in both cases they contain some older commercial buildings which under-utilize the properties they occupy, even under current zoning. In the NEWBA, these buildings are found primarily along the Bothell-Everett Highway: in the SOBA, they are located mainly along Juanita Drive, 100th Avenue NE, 124th Avenue NE and NE 124th Street.

Commercial redevelopment potential is greater in the SOBA than the NEWBA because the former contains more land in commercial use. When such redevelopment might occur is not predictable with any certainty.

2. What are the projected capital expenses in the SOBA?

An analysis prepared by the City of Kirkland in September 2007 identified \$18.8 million of road and storm water projects in the SOBA. In November 2007, King County responded with an offer of completion of certain road and surface water management projects. Staff will obtain a copy of the September 2007 project list to determine if any of the projects have been completed or are funded and will be completed by King County in the near term.

Staff is also checking all bridge inspection records to determine if all bridge deficiencies are included in the \$18.8 million figure.

There is a large drainage project identified as "Billy Creek" that is under study by King County Water and Land Resource Division. Staff will confirm the scope of the project and if the solution included in the \$18.8 million figure is still accurate.

In general, the overall conditions of the existing roadway pavements are comparable in the NEWBA, the SOBA, and current City limits. Neither annexation should require an immediate expenditure of City overlay funding that would be detrimental to the existing City residents.

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3. Would King County offer a financial incentive for the SOBA? Would Snohomish County offer one for the NEWBA?

King County has in the past offered Kirkland a one-time payment of \$2.5 million if it would annex its northern PAA, comprising Finn Hill, Upper Juanita and Kingsgate. The City's financial analysis at this point assumes that King County will be willing to provide Bothell the same amount as the result of annexation.

Snohomish County has not historically offered financial incentives to its cities to annex unincorporated territory. Nevertheless, insofar as an annexation as large as the NEWBA would relieve the County of substantial service responsibilities, the City Manager has transmitted a letter to Snohomish County Executive Reardon suggesting that such an incentive would be mutually beneficial to the County and the City (see **Attachment 2**).

4. What is Kirkland's timetable for deciding whether to retain or relinquish its Potential Annexation Area (PAA)?

The Kirkland Council is scheduled to resume discussion of retention or relinquishment of its PAA, and annexation of the PAA, at its March 3 meeting. Staff has received no indication that the Kirkland Council would discuss this topic before then. It is also not known if Kirkland will provide any definitive response related to annexation at this meeting.

5. Why have the Police and Fire departments projected higher expenses within the SOBA than the Nesbitt fiscal analysis forecasted?

Fire Department response. There are two reasons the Fire Chief's staffing figures differ from the consultant's.

First, although the consultant's figures are based on comparative analysis, i.e. assessed valuation, population, calls for service, etc., the Chief believes the consultant did not take the physical characteristics of the area to be covered into consideration.

The City of Kirkland Fire Department completed a study that determined they could cover their PAA from two stations, instead of the three currently in place. The Kirkland Fire Department concluded that to cover the area with two stations, one of them would have to be strategically relocated.

Since the proposed annexation includes an area currently covered by a Woodinville fire station, as well as the three from Kirkland, the Chief is confident that responding to the area from two stations will provide the same level of service the citizens in the annexation area now receive.

Second, taking into account the City's contractual obligations with our Fire Department personnel for vacation, holiday and other leaves, 11.99 FTEs (rounded to 12) are necessary to staff one fire engine 24/7 at each station. Although the consultant's model suggests fewer personnel, the Chief's analysis indicates the City would need 24 FTE's to staff the two stations necessary to provide service to the SOBA.

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Please note that the Chief's proposal recommends 20 FTEs. He believes that the Department can reassign four FTEs from the Downtown Firehouse to assist in staffing the two stations in the SOBA. Some of the call volume currently handled by the Downtown crews could be covered by one of these stations, recognizing to some degree the consultant's analysis.

Police Department response. The Police Chief is recommending additional personnel to ensure that the City's level of service provided to the SOBA will be the same as currently provided to the City of Bothell.

He is concerned that the consultant's recommended staffing level could detract from the level of service currently received by Bothell citizens. The Chief is also recommending additional staffing to ensure the Department's supervisory structure is able to retain both a manageable span of control and a desired level of quality in its service delivery.

As was stated in the Fire Chief's response to this question, the SOBA has difficult transportation routes (particularly east/west routes), making police response times challenging, thus emphasizing the need to keep officers in their districts.

Historically, police activity has been higher in the Kingsgate area than the other two SOBA areas (Juanita, Finn Hill), necessitating assigning two officers to that district. Also, the Kingsgate area has unique characteristics, such as larger business districts, a card room, and a hospital and emergency room nearby.

The Department is aware that Kingsgate will also be home to an automobile dealership, which will result in additional calls for service. The only new police service the Chief is recommending in addition to what current citizens have now would be a tracking K-9 unit. This unit would be necessary due to the number of events needing that type of service.

6. What advantages and disadvantages has staff identified for the SOBA and NEWBA?
(Please note that the responses below do not include or reiterate the financial analysis conducted on these two areas)

NEWBA Pros:

- A substantial number of citizens in the NEWBA have evidenced support for annexation to become part of Bothell. NEWBA residents are currently within Bothell's MUGA.
- Staff is familiar with the proposed annexation area: the area involves the same drainage basins; has predominantly Bothell postal addresses; and is predominantly within the Northshore School District.
- Due to the above, the area may have "built-in" citizen support for current and future city projects. Since they already identify with Bothell, NEWBA citizens may be more willing than SOBA residents to vote for the good of the city on financial issues.
- Fire already provides service to roughly half of this area through contract with Fire District 10. Providing service to the remainder is less of an impact than starting new

Agenda Staff Report
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with the entire area. Fire and Police do not anticipate problems in protecting the NEWBA. There are multiple north/south access points into the NEWBA, providing faster access for emergency response. Needed new police officers could be housed in the current police facility rather than needing a satellite station.

- The new Public Works maintenance facility is being built very close to our existing northern boundary, which makes it advantageously located to serve the NEWBA.

NEWBA Cons:

- Neighboring fire jurisdictions are dispatched by a different dispatch center than the City of Bothell, making mutual aid requests slower due to incompatible technology. Even with improved station locations, some areas of the NEWBA will be in the five-minute or more response range, near the limit of acceptable response time. Neighboring fire jurisdictions are under a different medical license than King County, sometimes causing minor confusion on EMS-related calls.
- The large number of multi-family dwellings along the SR 527 corridor could generate more police activity.
- There is little opportunity for sales-tax-generating commercial development, as most of the NEWBA is zoned for residential uses.

SOBA Pros:

- Numerous existing fire stations. Depending upon what facilities are acquired, annexation could provide multiple fire station location options. Neighboring fire jurisdictions are able to provide adequate mutual aid into the SOBA. Neighboring fire jurisdictions are dispatched from the same dispatch center, providing faster response to requests for automatic or mutual aid. Neighboring fire jurisdictions are under the same medical program, making for easier cooperative work on EMS calls. Annexation would solve an existing City response time issue near Simonds Rd.
- SOBA has extensive Lake Washington waterfront and additional park lands that could enhance the City's appeal and attraction.
- SOBA would give Bothell a larger presence on the Eastside and in King County, and thus more influence on transportation and other regional issues. The City would extend into additional County and State legislative districts.
- The Bothell Public Works Department enjoys a good working relationship with the Kirkland Public Works Department: both departments are full service and like-minded. Bothell has a good working relationship with the Northshore Utility District.

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SOBA Cons:

- SOBA citizens may not as readily identify with Bothell as much as they do with Kirkland. Most of the SOBA has Kirkland postal addresses and is in the Lake Washington School District. Accordingly, SOBA citizens may not frequent downtown Bothell, and may not be as supportive of future funding measures to achieve Bothell citizens' current Vision for Downtown.
 - Public Works would need to perform analysis of property along the waterfront to assess the potential for landslides.
 - There might not be time enough to "commence" annexation, especially if Kirkland does not release the PAA, thereby failing to qualify for the State STI.
7. **How do the SOBA and NEWBA compare in number, type and size of parks, bridges and other public facilities?**

Staff will provide this information at the February 10 Study Session, if not earlier.

Explanation of revised revenue / expenditure spreadsheet comparing NEWBA and SOBA

At the Council's January 13, 2009, Study Session, staff presented comparative financial information for the NEWBA and the SOBA.

In our continuing analysis of these two annexation opportunities, staff discovered that the estimated State Sales Tax Incentive (STI) figures were overstated for both the NEWBA and SOBA, and that the consultant's one-time annexation start-up cost amortization figures did not include associated interest.

Additionally, the consultant's study for each area assumed one-time costs being amortized over a three-year period, and the financial information presented to Council on January 13 incorporated three-year NEWBA and SOBA amortization schedules. As staff explained at the prior study session, the length of the amortization schedule is a Council policy decision.

The Finance Director has recommended applying a less aggressive ten-year amortization schedule to absorb the decrease in the estimated STI, as well as the addition of amortization interest over the same period.

Consequently, staff distributed a revised spreadsheet and memo to Council on January 20 which reflects the adjusted STI, as well as amortization interest (4%) for both the NEWBA and SOBA annexation areas, based on both a three-year and a ten-year amortization schedule (see **Attachment 3**). This spreadsheet is provided again as part of this packet.

Update on NEWBA

At the urging of the Snohomish County Boundary Review Board (BRB) and to allow additional time to address two issues of interest to the City, Bothell staff has requested a 120-day extension to the

Agenda Staff Report
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BRB's statutory deadline for acting on the NEWBA. The original deadline for BRB action, based on the City's November 2008 submittal, was March 24, 2009: the extension would move the deadline to July 22, 2009. State law allows the BRB and a municipality to mutually decide on extensions of statutory deadlines.

The BRB asked the City to request an extension because the County Assessor's office required several iterations of review of the legal description before it was determined to be satisfactory. Since the BRB's policy is not to begin the 45-day comment period on a proposed annexation until the County Assessor approves the legal description, the BRB found itself with too little time to accommodate the comment period, hearing and decision prior to the original March 24 deadline.

The extension is advantageous to the City as well, as it provides more time to resolve the Bothell - Mill Creek minor MUGA boundary discrepancy described in the agenda bill for the prior Study Session (Mill Creek will be sending a letter to the BRB supporting Bothell's adopted MUGA boundary), and to achieve adoption by the City and County councils of a master annexation interlocal agreement.

Alternative scenario: pursue annexation of adopted PAA concurrent with NEWBA

It has been suggested that as an alternative to pursuing annexation of unincorporated Finn Hill, Upper Juanita and Kingsgate, currently within Kirkland's PAA, the Council may be interested in considering the NEWBA combined with annexing all of the unincorporated areas that comprise Bothell's PAA within King County.

Successfully doing so would expand incorporated Bothell out to the boundaries the City first established in the early 1990's (except for the Bothell - Brier MUGA boundary) as representing that area to which the City would logically provide urban services and in which the City desired to control or influence land use and infrastructure.

The unincorporated territory that comprises Bothell's PAA amounts to 1,003 acres and contains an estimated population (as of 2006) of 4,576. This territory is distributed geographically among three small "islands" on Westhill; one small island on Maywood Hill; two larger areas on the west and southwest slopes of Westhill; two large contiguous areas on south Norway Hill and east of I-405 in the Brickyard area; a small pocket on 124th Avenue NE; and one larger pocket on the northeast corner of Bloomberg Hill (see **Attachment 4**).

Unfortunately, under state law, each annexation must be capable of being described by one legal description which encloses the entire annexation: consequently, the various separated unincorporated areas which make up Bothell's PAA must each be processed as its own annexation.

If Council were to pursue annexation of all of the unincorporated territory comprising Bothell's PAA, staff estimates that nine (and possibly ten) annexations would need to be processed.

While this may appear to be a daunting number, state law does provide a streamlined process for annexing the islands: this process involves neither a petition nor an election. Even for the larger unincorporated areas, there are procedural options which could expedite certain steps of the annexation process.

Agenda Staff Report
 Subject: Continued Study Session to Consider Potential South of Bothell Annexation (SOBA)
 Meeting Date: February 10, 2009
 Staff Contact: Steve Anderson, Deputy City Manager

As to support for annexation within those areas, on the basis of inquiries over the past several years staff believes that citizen interest in annexing to Bothell is substantial and widespread throughout the PAA.

With respect to the financial aspects of annexing the PAA, the 2006 Nesbitt analysis divided the PAA and MUGA into smaller subareas and calculated likely revenues and costs. Staff has updated those numbers for 2009 as follows:

PAA Subarea	Unrestricted revenue	Operating costs	Net
Central infill (three islands on Westhill plus one island on Maywood Hill, totaling 23 acres)	\$21,097	\$105,180	-\$84,083
Westhill (two large pockets on Westhill, totaling 289 acres)	\$625,464	\$558,991	\$66,473
Waynita (south Norway Hill, totaling 475 acres)	\$1,056,712	\$915,895	\$140,817
Brickyard (east of I-405, straddling NE 160 th Street, totaling 183 acres)	\$512,533	\$764,625	-\$252,092*
Hollyhills (pocket on northeast portion of Bloomberg Hill, totaling 33 acres)	\$99,280	\$141,816	-\$42,536
Total	\$2,315,086	\$2,486,507	-\$171,422

* According to the Nesbitt report, the gap in the Brickyard subarea is primarily attributable to the expected cost of maintaining East Norway Hill Park, which could be viewed as a city-wide benefit.

Please note that the annexation sales tax incentive (STI) could be utilized to bridge the gap where there is a net deficit between revenue and costs, provided the annexations could be “commenced” before January 1, 2010. If “commencement” is construed as a Council action initiating consideration of an annexation - such as the resolution the Council adopted to formally initiate the NEWBA annexation - then all of the annexations within the PAA could be commenced by that deadline.

Should the Council decide to pursue this alternative, staff recommends the following approach:

1. A two- to three-month outreach effort to advise citizens within the PAA of the City’s interest in annexation. During this time staff can be compiling other information, such as legal descriptions, that would be needed later for processing the annexations.
2. Following the outreach, Council adoption of resolutions formally initiating the various annexations.

Activities subsequent to the above for each annexation would include:

- Preparation of a Notice of Intention to submit to the King County Boundary Review Board, followed by a Board hearing (if jurisdiction is invoked) and decision.
- Scheduling of an election (not required for the island annexations).
- Further outreach prior to the election.
- The election itself.
- Adoption of annexation ordinances.

January 29, 2009

The Honorable Aaron Reardon
Snohomish County Executive
3000 Rockefeller Avenue
M/S 407
Everett, WA 98201



Dear Executive Reardon:

In response to a citizen petition filed with Bothell City Council last year, the Council is currently evaluating the merits of a possible annexation via public vote of the City's Municipal Urban Growth Area (MUGA) in Snohomish County. The City has already filed its Notice of Intent with the Boundary Review Board for annexation for the area shown on the attachment. This area currently includes a resident population of over 20,000 people. In addition, we are currently working with County staff on a Master Interlocal Agreement addressing such issues of governance transition, permitting, and transference of capital mitigation dollars.

The Bothell City Council is also evaluating a potential annexation of even greater size in terms of population in unincorporated King County. The financial studies, which we have conducted for both of these potential annexation areas, indicate the need for financial assistance from the State in the form of the State's Sales Tax Incentive program to offset operating expenses and the need for a funding source to pay for infrastructure and other capital investments needed in both unincorporated areas.

King County has recognized for years the financial strain it has placed upon its resources in an attempt to provide urban level services to unincorporated areas. King County has also recognized that in order to promote a financial solution for itself and encourage cities to assume the costly support of these areas via annexation, a financial incentive package needed to be created and offered to cities. If Bothell decides to move forward with the proposed annexation to the south in King County, it is anticipated that King County will financially contribute toward the annexation via an interlocal agreement. For reference, King County offered the City of Kirkland an amount of \$2.5 million to offset some much needed operational and capital costs associated with a proposed annexation in 2008 of the same area as Bothell is currently evaluating today.

Having served Snohomish County cities since 1990, I believe the same financial drain on Snohomish County resources is occurring in order to provide an urban level of service to its unincorporated areas. I am confident that you would find an ultimate savings in focusing County resources toward the provision of regional services if cities could be encouraged to annex areas within their MUGA's with the assistance of one-time funds provided by Snohomish County.

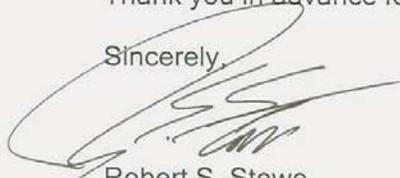
18305 101st Ave. NE
Bothell, WA 98011
425.486.3256
www.ci.bothell.wa.us

The Honorable Aaron Reardon
Page 2
January 29, 2009

As Bothell continues its evaluation of which annexation makes the most financial sense, I am respectfully requesting that Snohomish County consider making a similar financial incentive package available. I would be happy to meet with you to further discuss this request or to assemble other cities to meet with you on this important matter.

Thank you in advance for considering this request.

Sincerely,

A handwritten signature in black ink, appearing to read "R. Stowe", written over a horizontal line.

Robert S. Stowe
City Manager

c: Bothell City Council

MEMORANDUM
Office of the City Manager



DATE: February 4, 2009
TO: Mayor & Council
CC: Robert S. Stowe, City Manager
FROM: Stephen L. Anderson, Deputy City Manager
SUBJECT: Annexation Areas

At your January 13, 2009 study session, staff presented financial information regarding the potential annexation areas described as North, East and West of Bothell Area (NEWBA) and South of Bothell Area (SOBA).

In staff's continuing analysis of these two annexation opportunities, we discovered that the estimated State Sales Tax Incentive (STI) figures were overstated for both the NEWBA and SOBA, and that the consultant's one-time annexation start up cost amortization figures did not include associated interest. The attached spreadsheets reflect the adjusted STI, as well as amortization interest (4%) for both the NEWBA and SOBA annexation areas.

The consultant's study for each area depicted one-time costs being amortized over a three-year period. As we explained at your study session, the amortization schedule is a Council policy decision.

The financial information presented to you on January 13, included the consultant's three-year NEWBA and SOBA amortization schedules. The attached spreadsheets include both a three-year and a ten-year amortization schedule. The Finance Director's January 20, 2009 memo to the Council recommended applying a less aggressive ten-year amortization schedule to absorb the decrease in the estimated STI, as well as the addition of amortization interest over the same period.

18305 101st Ave.
NE
Bothell, WA 98011

425.486.3256
www.ci.bothell.wa.us
s

EXHIBIT 2
Revised 2/4/2009 1:48 PM

SOBA Revenues / Expenses
3 year Amortization Analysis

Revenue Sources:	Unrestricted Op Revenues as per Nesbitt Study	OP Rev	OP Rev + Sales Tax Incentive	OP Rev + Sales Tax Incentive + Dealership - Norway Hill	Op Revs + Sales Tax Incentive + Dealership + Card Room - Norway Hill	YEAR 1 2009	YEAR 2 2010	YEAR 3 2011	YEAR 4 2012	Comparison of Year 1 SOBA to NEWBA	
										SOBA YEAR 1 2009	NEWBA YEAR 1 2009
Unrestricted OP Revenue ⁸	\$14,238,000	\$14,238,000	\$14,238,000	\$14,238,000	\$14,238,000	\$15,092,280	\$15,997,817	\$16,957,686		\$14,238,000	\$7,647,000
Dealership ²				\$350,000	\$350,000	\$371,000	\$393,260	\$416,856		\$350,000	NA
Card Room (11%) ³					\$580,000	\$614,800	\$651,688	\$690,789		\$580,000	NA
Sub-total Revenues	\$14,238,000	\$14,238,000	\$14,238,000	\$14,588,000	\$15,168,000	\$16,078,080	\$17,042,765	\$18,065,331		\$15,168,000	\$7,647,000
Operating Expenses per Nesbitt ⁸	\$14,613,000	\$14,613,000	\$14,613,000	\$14,613,000	\$14,613,000	\$15,470,000	\$16,708,500	\$17,700,600		\$14,613,000	\$7,034,852
Fire and Police Expense Adds ^{5,8,12}		\$2,252,359	\$2,252,359	\$2,252,359	\$2,252,359	\$1,883,999	\$2,015,879	\$2,156,991		\$2,252,359	
3 year Deficit Amortization Amount ⁷		\$2,003,680	\$2,003,680	\$2,003,680	\$2,003,680	\$2,003,680	\$2,003,680	\$2,003,680		\$2,003,680	\$1,736,000
Norway Hill Deficit ⁶				\$175,282	\$175,282	\$185,799	\$196,947	\$208,764		\$175,282	\$0
Sub-total Expenses	\$14,613,000	\$16,616,680	\$18,869,039	\$19,044,321	\$19,543,478	\$20,925,006	\$20,066,354	\$20,066,354		\$19,044,321	\$8,770,852
Net after Expenses	-\$375,000	-\$2,378,680	-\$4,631,039	-\$4,456,321	-\$3,876,321	-\$3,465,398	-\$3,882,241	-\$2,001,024		-\$3,876,321	-\$1,123,852
State Sales Tax Incentive (STI) ¹⁰			\$3,064,708	\$3,064,708	\$3,064,708	\$3,092,290	\$3,290,197	\$3,510,640		\$3,064,708	\$2,990,000
Net after utilizing STI funding	-\$375,000	-\$2,378,680	-\$1,566,331	-\$1,391,613	-\$811,613	-\$373,108	-\$592,044	\$0		-\$811,613	\$0
STI funds unused & available¹¹								\$1,509,616			\$1,866,148

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SOBA Revenues / Expenses
3 year Amortization Analysis

- ¹ Not used
- ² Dealership relocation expected to generate between \$200,000 and \$500,000; used estimate of \$350,000
- ³ City currently bans card rooms. Options might include Interlocal Agreement with King County or pre-annexation agreement with operator
- ⁴ Not used
- ⁵ Fire and Police Expense Adds recommended by Chiefs
- ⁶ Norway Hills - reflects Waynita net Revenue of \$76,500 and Brickyard deficit of -\$233,100, for net negative figure of -\$156,600. Then updated to 2009 figure of -\$175,282
- ⁷ Nesbitt Study amortization amount did not include interest. Applied simple interest at 4%.
- ⁸ Multiplier of 1.06 percent applied to revenues. Multiplier applied to Expenses based on Puget Sound Economic Forecaster
- ⁹ NEWBA Operating Expenses \$6,332,000 (Nesbitt crosswalk) were increased by 1.111% to adjust for inflation to become \$7,034,852.
- ¹⁰ STI funds for SOBA Year 1 - 2009 reflect \$2,714,000 for current city boundary plus \$350,708 for the annexed area. Puget Sound Economic Forecaster was used to account for subsequent years' changes.
- ¹¹ STI funds unused are available only towards increased/unforeseen annexation-related expenses
- ¹² Fire and Police Adds for Years 2-12 do not include one-time expenses, and do include the multiplier of 1.07 percent

King County offered Kirkland a one-time payment of \$2,500,000 as incentive to annex this area. These monies may be dedicated to future needs. The agreement between King County and Kirkland has expired.

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SOBA Revenues / Expenses
10 year Amortization Analysis

Revenue Sources:	Unrestricted Op Revenues as per Nesbitt Study	OP Rev	OP Rev + Sales Tax Incentive	OP Rev + Sales Tax Incentive + Dealership - Norway Hill	Op Revs + Sales Tax Incentive + Dealership + Card Room - Norway Hill YEAR 1 2009	YEAR 2 2010	YEAR 3 2011	YEAR 4 2012	Comparison of Year 1 SOBA to NEWBA
Unrestricted OP Revenue ⁸	\$14,238,000	\$14,238,000	\$14,238,000	\$14,238,000	\$14,238,000	\$15,092,280	\$15,997,817	\$16,957,686	SOBA YEAR 1 2009 \$14,238,000
Dealership ²				\$350,000	\$371,000	\$393,260	\$416,856		NEWBA YEAR 1 2009 \$350,000 NA
Card Room (11%) ³					\$614,800	\$651,688	\$690,789		NEWBA YEAR 1 2009 \$580,000 NA
Sub-total Revenues	\$14,238,000	\$14,238,000	\$14,238,000	\$14,588,000	\$16,078,080	\$17,042,765	\$18,065,331		\$15,168,000 \$7,647,000
Operating Expenses per Nesbitt ⁸	\$14,613,000	\$14,613,000	\$14,613,000	\$14,613,000	\$15,470,000	\$16,708,500	\$17,700,600		SOBA YEAR 1 2009 \$14,613,000
Fire and Police Expense Adds ^{5,8,12}			\$2,252,359	\$2,252,359	\$1,883,999	\$2,015,879	\$2,156,991		NEWBA YEAR 1 2009 \$2,252,359
10 year Deficit Amortization Amount ⁷		\$751,380	\$751,380	\$751,380	\$751,380	\$751,380	\$751,380		SOBA YEAR 1 2009 \$751,380
Norway Hill Deficit ⁶				\$175,282	\$185,799	\$196,947	\$208,764		NEWBA YEAR 1 2009 \$175,282
Sub-total Expenses	\$14,613,000	\$15,364,380	\$17,616,739	\$17,792,021	\$18,291,178	\$19,672,706	\$20,817,734		\$17,792,021 \$7,685,852
Net after Expenses	-\$375,000	-\$1,126,380	-\$3,378,739	-\$3,204,021	-\$2,213,098	-\$2,629,941	-\$2,752,404		-\$2,624,021 -\$38,852
State Sales Tax Incentive (STI) ¹⁰			\$3,064,708	\$3,064,708	\$3,092,290	\$3,290,197	\$3,510,640		SOBA YEAR 1 2009 \$3,064,708
Net after utilizing STI funding	-\$375,000	-\$1,126,380	-\$314,031	-\$139,313	\$0	\$0	\$0		NEWBA YEAR 1 2009 \$0
STI funds unused & available ¹¹				\$440,687	\$879,192	\$660,256	\$758,236		SOBA YEAR 1 2009 \$440,687
									NEWBA YEAR 1 2009 \$2,951,148

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SOBA Revenues / Expenses
10 year Amortization Analysis

- ¹ Not used
- ² Dealership relocation expected to generate between \$200,000 and \$500,000; used estimate of \$350,000
- ³ City currently bans card rooms. Options might include Interlocal Agreement with King County or pre-annexation agreement with operator
- ⁴ Not used
- ⁵ Fire and Police Expense Adds recommended by Chiefs
- ⁶ Norway Hills - reflects Waynita net Revenue of \$76,500 and Brickyard deficit of -\$233,100, for net negative figure of -\$156,600. Then updated to 2009 figure of -\$175,282
- ⁷ Nesbitt Study amortization amount did not include interest. Applied simple interest at 4%.
- ⁸ Multiplier of 1.06 percent applied to revenues. Multiplier applied to Expenses based on Puget Sound Economic Forecaster
- ⁹ NEWBA Operating Expenses \$6,332,000 (Nesbitt crosswalk) were increased by 1.111% to adjust for inflation to become \$7,034,852
- ¹⁰ STI funds for SOBA Year 1 - 2009 reflect \$2,714,000 for current city boundary plus \$350,708 for the annexed area. Puget Sound Economic Forecaster was used to account subsequent years' changes.
- ¹¹ STI funds unused are available only towards increased/unforeseen annexation-related expenses
- ¹² Fire and Police Adds for Years 2-12 do not include one-time expenses, and do include the multiplier of 1.07 percent

King County offered Kirkland a one-time payment of \$2,500,000 as incentive to annex this area. These monies may be dedicated to future needs. The agreement between King County and Kirkland has expired.

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Comparison of NEWBA to SOBA
Years 1 - 11 and 10 Year Deficit Amortization

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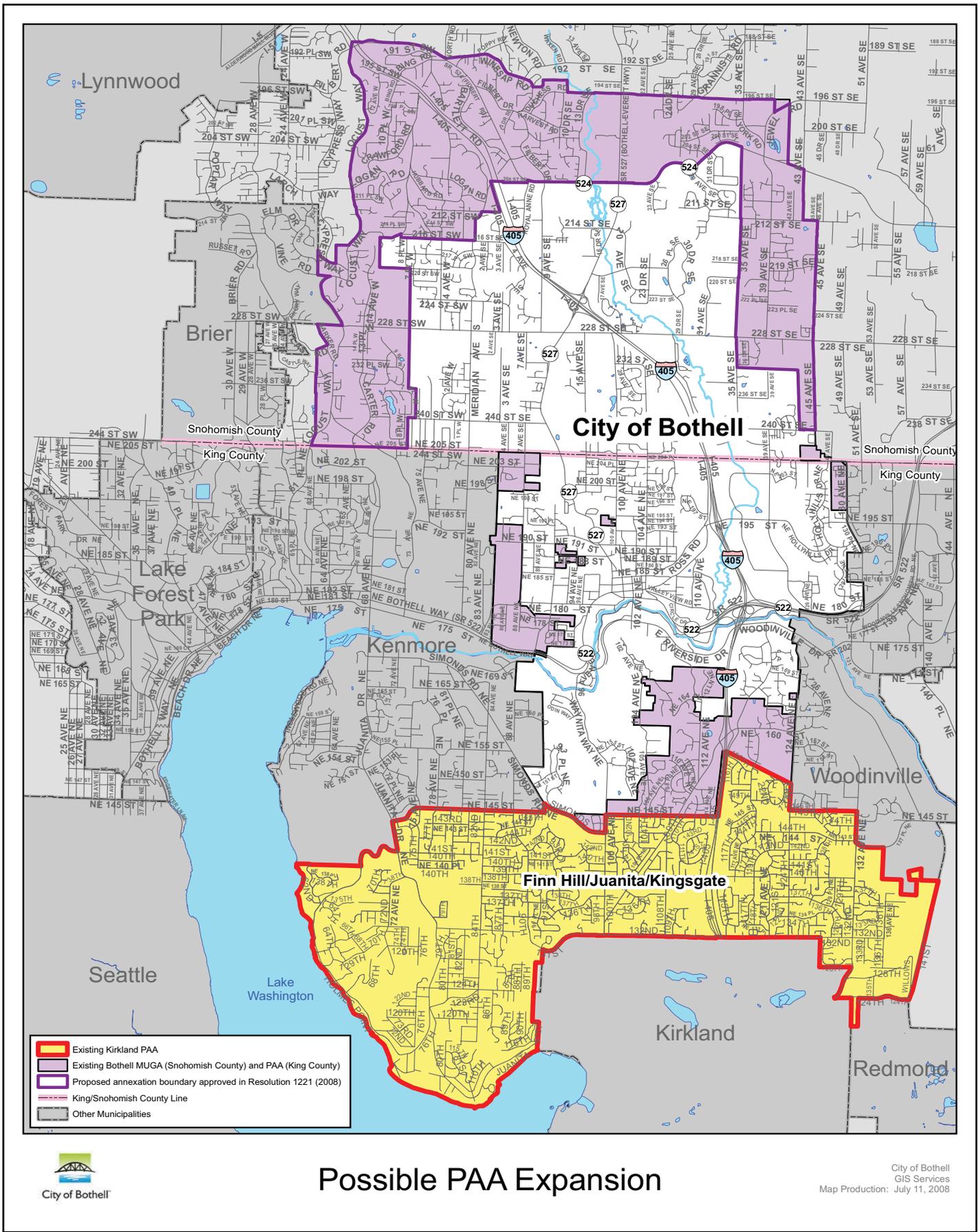
Revenue Sources:	SOBA YEAR 1 2009	NEWBA YEAR 1 2009	SOBA YEAR 2 2010	NEWBA YEAR 2 2010	SOBA YEAR 3 2011	NEWBA YEAR 3 2011	SOBA YEAR 4 2012	NEWBA YEAR 4 2012
Op Revs + Sales Tax Incentive + Dealership + Card Room - Norway Hill								
Unrestricted OP Revenue ⁸	\$14,238,000	\$7,647,000	\$15,092,280	\$8,105,820	\$15,997,817	\$8,592,169	\$16,957,686	\$9,107,699
Dealership ²	\$350,000	NA	\$371,000	NA	\$393,260	NA	\$416,856	NA
Card Room (11%) ³	\$580,000	NA	\$614,800	NA	\$651,688	NA	\$690,789	NA
Sub-total Revenues	\$15,168,000	\$7,647,000	\$16,078,080	\$8,105,820	\$17,042,765	\$8,592,169	\$18,065,331	\$9,107,699
Operating Expenses per Nesbitt ⁸	\$14,613,000	\$7,034,852	\$15,470,000	\$7,414,424	\$16,708,500	\$7,819,166	\$17,700,600	\$8,251,578
Fire and Police Expenses Adds ^{5,8,12}	\$2,252,359		\$1,883,999		\$2,015,879		\$2,156,991	
10 year Deficit Amortization Amount ¹³	\$751,380	\$651,000	\$751,380	\$651,000	\$751,380	\$651,000	\$751,380	\$651,000
Norway Hill Deficit ⁶	\$175,282		\$185,799		\$196,947		\$208,764	
Sub-total Expenses	\$17,792,021	\$7,685,852	\$18,291,178	\$8,065,424	\$19,672,706	\$8,470,166	\$20,817,735	\$8,902,578
Net after Expenses	-\$2,624,021	-\$38,852	-\$2,213,098	\$40,396	-\$2,629,941	\$122,003	-\$2,752,404	\$205,121
State Sales Tax Incentive (STI) ¹⁰	\$3,064,708	\$2,990,000	\$3,092,290	\$3,016,910	\$3,290,197	\$3,209,992	\$3,510,640	\$3,425,062
Net	\$0	\$0	\$0	\$40,396	\$0	\$122,003	\$0	\$205,121
STI funds unused & available ¹¹	\$440,687	\$2,951,148	\$879,192	\$3,016,910	\$660,256	\$3,209,992	\$758,236	\$3,425,062

EXHIBIT 2
Comparison of NEWBA to SOBA
Years 1 - 11 and 10 Year Deficit Amortization
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Revenue Sources:	SOBA YEAR 5 2013	NEWBA YEAR 5 2013	SOBA YEAR 6 2014	NEWBA YEAR 6 2014	SOBA YEAR 7 2015	NEWBA YEAR 7 2015	SOBA YEAR 8 2016	NEWBA YEAR 8 2016
Unrestricted OP Revenue ⁸	\$17,975,147	\$9,654,161	\$19,053,656	\$10,233,411	\$20,196,875	\$10,847,416	\$21,408,688	\$11,498,261
Dealership ²	\$441,867	NA	\$468,379	NA	\$496,482	NA	\$526,271	NA
Card Room (11%) ³	\$732,237	NA	\$776,171	NA	\$822,741	NA	\$872,106	NA
Sub-total Revenues	\$19,149,251	\$9,654,161	\$20,298,206	\$10,233,411	\$21,516,098	\$10,847,416	\$22,807,064	\$11,498,261
Operating Expenses per Nesbitt ⁸	\$18,762,636	\$8,746,673	\$19,888,394	\$9,271,473	\$21,081,698	\$9,827,761	\$22,346,600	\$10,417,427
Fire and Police Expenses Adds ^{5,8,12}	\$2,307,980		\$2,469,539		\$2,642,406		\$2,827,375	
10 year Deficit Amortization Amount	\$751,380	\$651,000	\$751,380	\$651,000	\$751,380	\$651,000	\$751,380	\$651,000
Norway Hill Deficit ⁶	\$221,290		\$234,567		\$248,641		\$263,560	
Sub-total Expenses	\$22,043,286	\$9,397,673	\$23,343,880	\$9,922,473	\$24,724,126	\$10,478,761	\$26,188,914	\$11,068,427
Net after Expenses	-\$2,894,035	\$256,489	-\$3,045,675	\$310,938	-\$3,208,028	\$368,654	-\$3,381,851	\$429,833
State Sales Tax Incentive (STI) ¹⁰	\$3,721,278	\$3,630,566	\$3,944,555	\$3,848,400	\$4,181,228	\$4,079,304	\$4,432,102	\$4,324,062
Net	\$0	\$256,489	\$0	\$310,938	\$0	\$368,654	\$0	\$429,833
STI funds unused & available ¹¹	\$827,243	\$3,630,566	\$898,881	\$3,848,400	\$973,201	\$4,079,304	\$1,050,252	\$4,324,062

EXHIBIT 2
Comparison of NEWBA to SOBA
Years 1 - 11 and 10 Year Deficit Amortization
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Revenue Sources:	SOBA YEAR 9 2017	NEWBA YEAR 9 2017	SOBA YEAR 10 2018	NEWBA YEAR 10 2018	SOBA YEAR 11 2019	NEWBA YEAR 11 2019	SOBA YEAR 12 2020	NEWBA YEAR 12 2020
Unrestricted OP Revenue ⁸	\$22,693,209	\$12,188,156	\$24,054,801	\$12,919,446	\$25,498,090	\$13,694,612	\$27,027,975	\$14,516,289
Dealership ²	\$557,847	NA	\$591,318	NA	\$626,797	NA	\$664,404	NA
Card Room (11%) ³	\$924,432	NA	\$979,898	NA	\$1,038,692	NA	\$1,101,013	NA
Sub-total Revenues	\$24,175,488	\$12,188,156	\$25,626,017	\$12,919,446	\$27,163,578	\$13,694,612	\$28,793,393	\$14,516,289
Operating Expenses per Nesbitt ⁸	\$23,687,396	\$11,042,473	\$25,108,639	\$11,705,021	\$26,615,158	\$12,407,322	\$28,212,067	\$13,151,762
Fire and Police Expenses Adds ^{5,8,12}	\$3,025,291		\$3,237,062		\$3,463,656		\$3,706,112	
10 year Deficit Amortization Amount	\$751,380	\$651,000	\$751,380	\$651,000				
Norway Hill Deficit ⁶	\$279,373		\$296,136		\$313,904		\$332,738	
Sub-total Expenses	\$27,743,440	\$11,693,473	\$29,393,217	\$12,356,021	\$30,392,717	\$12,407,322	\$32,250,917	\$13,151,762
Net after Expenses	-\$3,567,953	\$494,683	-\$3,767,200	\$563,425	-\$3,229,140	\$1,287,290	-\$3,457,525	\$1,364,527
State Sales Tax Incentive (STI) ¹⁰	\$4,698,028	\$4,583,506	\$4,979,910	\$4,858,516	\$0	\$0	\$0	\$0
Net	\$0	\$494,683	\$0	\$563,425	-\$3,229,140	\$1,287,290	-\$3,457,525	\$1,364,527
STI funds unused & available¹¹	\$1,130,076	\$4,583,506	\$1,212,710	\$4,858,516	\$0	\$0	\$0	\$0



Possible PAA Expansion



City of Bothell
GIS Services
Map Production: July 11, 2008