



CITY OF KIRKLAND
Department of Finance & Administration
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MEMORANDUM

To: David Ramsay, City Manager

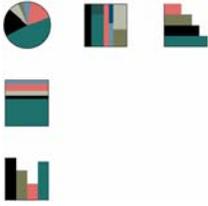
From: Tracey Dunlap, Director of Finance and Administration

Date: October 7, 2008

Subject: Kirkland Tax Burden Study Update

At the August 5, 2008 City Council meeting, the Council directed staff to update the Tax Burden Study with the assumed tax rate increases that will occur in 2009 and 2010 and show the impact of alternate business tax amounts. The attached memorandum from Berk and Associates summarizes the results. The full draft of the Tax Burden study report can be found as part of the August 5 packet on the City's website at: http://www.ci.kirkland.wa.us/_shared/assets/10a_NewBusiness9454.pdf.

The consultants will be in attendance at the October 21 City Council meeting to discuss the Tax Burden Study and this supplemental information.



ATTACHMENT A

MEMORANDUM

DATE: October 13, 2008

TO: Tracey Dunlap, City of Kirkland

FROM: Michael Hodgins

RE: **Tax Burden Implications of Proposed New Taxes
Addendum to Tax Burden Study**

The following memorandum provides an assessment of how the proposed changes in City tax policy would likely affect the distribution of tax burden. The analysis was conducted using the updated City Tax Burden Study as a baseline estimate of the tax burden for a number of representative taxpayers in the City of Kirkland. The following proposed tax policy changes were evaluated:

- Increase the utility taxes on public utilities from 7.5% to 10.5%.
- Increase the utility taxes on private utilities from 6% to 7.5% (would require a public vote to implement)
- Increase the property tax levy by using the remaining banked levy capacity (would add approximately \$145,000 to the City property tax collections)
- Replace the current business license surcharge with a per employee fee structure:
 - Current structure includes a \$100 License fee plus:
 - \$125 – businesses with a single employee
 - \$225 – businesses with 2-5 employees
 - \$750 – businesses with 6-20 employees
 - \$1,500 – businesses with 21-100 employees
 - \$2,500 – businesses with more than 100 employees
 - New structure would combine the current \$100 License fee with a surcharge of \$90 per employee

To analyze the impact of these proposed changes, we used the estimate of the current tax burden (2008) for the each of the representative taxpayers and estimate how these tax burdens would change assuming the new policies were in effect in 2008.

The results of this analysis are presented in **Exhibit 1**. The table shows, for 2008, the total tax burden for each of the representative taxpayers, the City of Kirkland burden, City share of total tax burden and the per capita City burden, where per capita is per resident for residential taxpayers and per job for commercial taxpayers. The impacts are shown in terms of what the City tax burden would have been if the new taxes were in place in 2008, both in terms of total City burden and per capita. The final portion of the table shows the change in estimated City taxes resulting from the change in tax policy and how these changes compare with the total tax burden (taxes to all jurisdictions).

Exhibit 1
Impact of Proposed City Tax Policy Changes
Comparison of 2008 Estimated Tax Burden with and without Proposed Changes

	2008 Actual Tax Burdens				Impact of Proposed Tax Changes			
	Total Tax Burden	City Tax Burden	City Share of Total Burden	City Burden per Capita	City Tax Burden, new taxes	City per Capita, new taxes	Change in City Taxes	% Change in Total Burden
Single Family HH	12,433	1,869	15%	692	2,048	758	179	1.4%
Condo HH	7,625	1,120	15%	747	1,227	818	107	1.4%
Apartment HH	3,865	648	17%	499	733	564	85	2.2%
Home Business	1,213	347	29%	347	323	323	-24	-2.0%
Grocery	123,803	14,079	11%	217	21,377	329	7,298	5.9%
Auto Dealer	323,648	18,448	6%	246	27,196	363	8,749	2.7%
Furniture Store	14,476	2,926	20%	418	3,233	462	307	2.1%
Electronics Store	25,055	3,223	13%	403	3,680	460	458	1.8%
Restaurant	55,630	12,296	22%	216	18,079	317	5,783	10.4%
Big Box Retailer	287,333	55,705	19%	338	80,988	491	25,283	8.8%
Engineering Firm	196,241	11,346	6%	258	15,208	346	3,861	2.0%
Office, Large	411,744	35,826	9%	239	51,603	344	15,777	3.8%
Office, Medium	182,545	11,346	6%	258	15,208	346	3,861	2.1%
Office, Small	36,974	3,065	8%	307	3,534	353	468	1.3%

The following are some general observations regarding this analysis:

- Not surprisingly, the impacts of the proposed changes would be disproportionately felt by the commercial taxpayers in the City. This is a function of two key factors:
 - All of the proposed changes will affect commercial taxpayers
 - The residential taxpayers would be unaffected by the proposed changes in the business license fee structure
- The impacts on the residential taxpayers would come from the utility and property tax changes and would result in an overall tax burden increase of between 1.4% and 2.2%.
- In dollar terms, the impacts to the residential taxpayers would be largest to the single family household; however the total increase in tax burden would be less than 2%. This is a result of the fact that the utility tax is the primary source of new tax burden, while the property tax is the largest portion of the single family tax burden.
- Earlier this year, City staff estimated that the proposed changes would result in an increase of \$9.65 per month for the average Kirkland household. The tax burden study is based on an updated set of assumptions for the household characteristics in the 2001 Tax Burden Study, which breaks representative households down into different types (single family, condos and

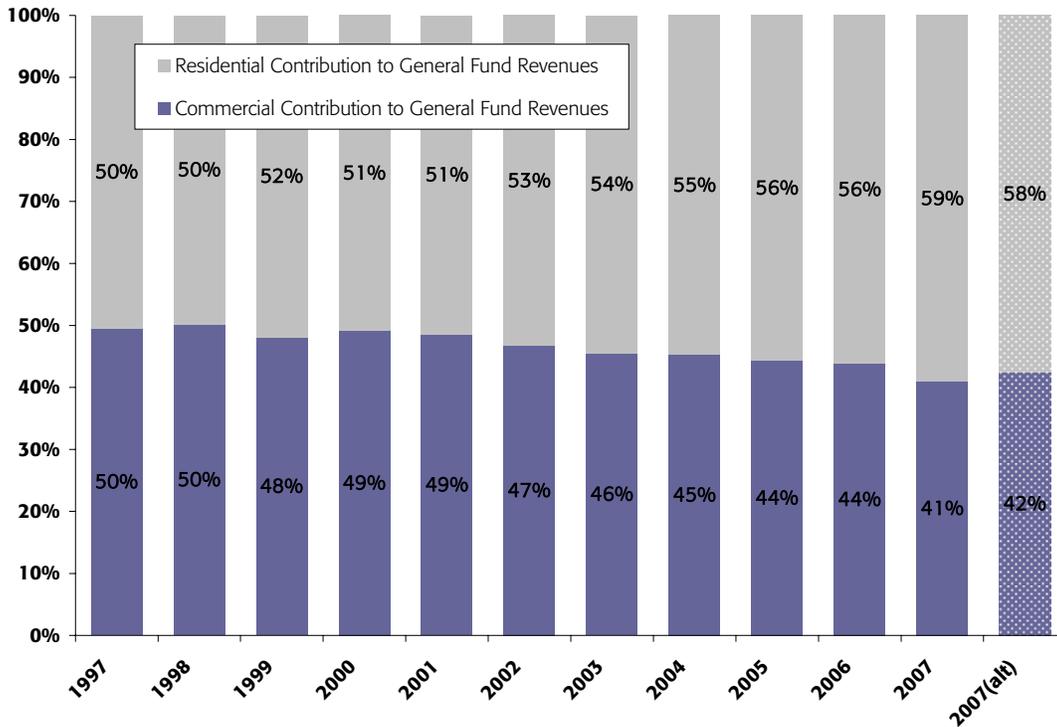
apartments). Based on these household types, the average monthly impact would vary from \$7.07 per month to \$14.91 per month. This range is attributable to variations in assessed values and utility purchases by household types, which can vary widely based on household incomes, household size and the size of the housing unit.

- The impacts are not uniformly distributed among the representative commercial taxpayers, with larger businesses experiencing the larger dollar increases in taxes. This is a function of the much more progressive business fee structure that is proposed. The impact on total tax burden of these changes on commercial taxpayers would range from -2% to 10%.
- The analysis suggests that one impact of the proposed changes is to reduce the variation among commercial taxpayers when you consider the local tax burden on a per employee basis. Currently the range is quite wide with the highest almost twice as high as the lowest (a low of \$216 per employee to a high of \$418 per employee). The result of the proposed changes is to reduce that gap almost in half, with the highest now only about 50% higher than the lowest (\$317 per employee versus \$491 per employee). Having a smaller range in this tax burden metric can be viewed as improving the equity of the local tax code, since the number of employees is one of the factors in the relative demand for local government services.
- The overall impact on tax burdens would vary widely from a net decrease in burden for a home based business to an increase of approximately 10% for a restaurant. This is a function of adding a per employee tax into an overall business tax structure in this state which is focused primarily on purchases (sales tax of which over 90% goes to other state and local agencies) and gross revenues (the state's B&O). As a result, businesses with relatively low gross sales per employee will see relatively higher percent changes in their overall tax burden.
- The analysis above focuses on a single option for the business license surcharge (\$100 fee plus \$90 per employee). A variant of this proposal has been discussed which would increase the per employee charge to \$100. The effect of this change on the tax burden assessment would be to increase the total tax burden for all commercial taxpayers an additional 0.2% to 1.0%.

Another area of interest regarding the proposed tax policy changes is the effect these changes might have on the overall tax contribution shares for residential and commercial. In the 2008 Tax Burden Study update, there was an assessment of the relative contributions of the residential and commercial components of the City's tax base. This analysis was added to more fully flesh out the issue of where the City's taxes come from, since it is possible for a group of taxpayers to have a relatively low tax burden individually, while at the same time these taxpayers cumulatively make a very large contribution to City revenues (assuming that there are many of these types of taxpayers).

The implications on the overall contribution shares for residential and commercial were evaluated using the last year of actual tax collections (2007) and comparing how total tax revenues might be affected if the new policies had been in place at that time. **Exhibit 2** presents the results of this analysis. The chart is an updated version of the contribution assessment chart used in the 2008 Tax Burden Study with one more "year" added. The last column shows the how the estimate of shares for 2007 collections would have changed under the proposed policies.

Exhibit 2
Impact of Proposed City Tax Policy Changes
Estimated Impact on Total Contribution Shares for Residential and Commercial



The analysis suggests that the resulting contribution shares would be shifted slightly toward the commercial tax base. Importantly, however, even with this shift, the commercial share would still have been lower than all previous years studied. This is largely consistent with the finding above, which noted that the commercial taxpayers would be affected by all of the proposed changes, while the residential tax payers would experience three of the four proposed changes. The following are some general observations regarding the potential impact on the contribution shares:

- The overall impact of the proposed changes on the contribution shares is relatively balanced due to the fact that 65% of the new revenues are coming from the utility and property tax changes. Because of the size of the City’s residential tax base, it contributes 70% of the utility taxes and 83% of the property taxes. So increases in these taxes will result in higher relative contributions from the residential base.
- The proposed changes to the business surcharge would obviously fall exclusively on the commercial base. So when the overall effects of the proposed changes are evaluated together, the contribution shares of the net increase in taxes would be 54% residential and 46% commercial.
- Since the proposal is somewhat more balanced than the overall contribution shares in 2007 (54%-46% versus 59%-41%) the analysis suggests that the changes would have had the effect of marginally making the overall shares more balanced.