CITY OF KIRKLAND
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MEMORANDUM

To: Kurt Triplett, City Manager

From: Ellen Miller-Wolfe, Economic Development Manager
David Godfrey, P.E., Transportation Manager
Ray Steiger, P.E., Interim Public Works Director

Date: January 6, 2011

Subject: Suspension of Change in Use Impact Fees

RECOMMENDATION

It is recommended that the City Council adopt the attached ordinance amending the Kirkland Municipal Code (KMC) to temporarily suspend the charging of impact fees for a "change in use" of an existing building through December 31, 2013.

BACKGROUND

At its 2010 Retreat, the City Council determined that economic development is both an important and urgent issue for Kirkland. In response to this concern, staff undertook a competitiveness study (Attachment 1) to understand how taxes and fee policies might be affecting the City's ability to remain competitive among its peer communities. While the study determined that the portion of locally variable costs that can be attributed to tax and fee policies is a relatively small share of these costs, it also indicated that a combination of the market and tax and fee costs make Kirkland one of the higher cost places in the region to do business. The consultants, Berk & Associates, indicated that targeting incentives toward new development and reducing historically high vacancy rates was important in this recessionary climate. One approach they suggested was to eliminate impact fees that are charged when a change of use results in an increase in SOV trips, but there is no related increase in square footage.

The Economic Development Committee (EDC), who studied this issue, asked if eliminating impact fees for changes of use could apply solely to specific business districts such as just in the Downtown area. It was determined that because the impact fee ordinance applied city-wide, it was legally challenging and inequitable to focus this incentive only on certain areas. In recognition of the current financial situation for the business community, the EDC recommended temporarily eliminating the charging of impact fees for change of use for the entire City at its November 22, 2010 meeting. It was recommended by the EDC at their November meeting that staff return to the full Council with an ordinance suspending the change of use impact fee.

State law authorizes the collection of impact fees to help defray the costs of new transportation infrastructure. Currently, the City collects impact fees on all new development including development/redevelopment of an existing structure from one use (i.e. furniture store) to another use (i.e. auto parts store). The attached ordinance authorizes the suspension until the City completes its next impact fee study likely to be completed in 2013. The suspension automatically expires on December 31, 2013.

Suspension of change of use impact fees will not affect the collection of impact fees for new development or the enlargement of existing buildings; it applies to a limited component of the development sector. It is estimated that change in use impact fees over the time since impact fees were first adopted, June of 1999, account for approximately 25-30% of all impact fees collected city-wide and for the 2011/2012 biennium, the potential loss of revenue is estimated to be approximately $250,000.

This loss in impact fees previously dedicated to CIP projects will require additional grant funding, other resources, or a delay in projects funded by the anticipated impact fees. At this time, the likely affected projects that are funded in part with impact fees in 2011/2012 are two signal projects associated with the NE 85th Street corridor improvements: 124th Ave NE, and 132nd Ave NE. Based on the current bidding climate in which bids are consistently 20 to 30% below the engineer's estimate, and as the 2012 construction of these improvements approaches, staff will modify the CIP projects accordingly.

City of Kirkland,
Economic Development

Competitiveness Assessment:
Cost of Doing Business in Kirkland

BERK & ASSOCIATES

OCTOBER 2010

OVERVIEW

Objective: To build on previous work (2008 Tax Burden Study) to explore the issue of the City of Kirkland's competitiveness to attract and retain business activity.

1. **Cost of Doing Business with Kirkland (Development Perspective).** The analysis of doing business with the City of Kirkland addresses how costs associated with permitting and impact fees compare with both other Cities cities and with overall costs of development. For similar projects, land costs and the costs of doing business with the host jurisdiction are the key locally-variable costs, while construction costs tend to be less variable site-to-site (excepting site prep/critical area issues).

2. **Cost of Doing Business in Kirkland (Business Owner/Operator Perspective).** The analysis of the business operator perspective considers the relative cost of doing business in the City of Kirkland. Beyond tax burdens, the analysis needs to consider lease rates, which are the other principal locally-variable business cost.

Peer Cities from 2008 Tax Burden Study

- Bellevue
- Bothell (King County Portion)
- Kent
- Redmond
- Renton

Representative Developments and Businesses

Representative Developments	Representative Businesses
Large Office	Large Office
Medium Office	Medium Office
Big Box Retail	Big Box Retailer
Strip Retail	Restaurant
Mixed Use (residential/retail)	

LOCAL COMPETITIVENESS AND THE MARKET PERSPECTIVE

How to Think About Local Competitiveness

- It is easy to focus too narrowly on relative costs associated with tax and fee policies -- the key question is whether these policies make a material difference to a location decision.
- Comparisons must be understood in a broader market context:
  - Costs of operating in any location are only relevant to the value of the location
  - Any meaningful differences in local tax and fee costs will be reflected in underlying land values

Current Market Considerations

- Generally, market pricing suggests that a Kirkland location is desirable in relation to some of its peer and neighbor cities.
- Relative to its peer and neighbor jurisdictions, the City of Kirkland has:
  - Higher land values for commercially-zoned land
  - Higher lease rates for office uses
  - Lower lease rates for retail uses
  - Much higher vacancy rates

Average Land Value per Square Foot, 2010
Commercially-zoned Land

City	2003	2007	2010
Bellevue (Outside of Downtown)	$13.93	$21.08	$38.41
Downtown Bellevue	*$70.32*	*$86.92*	*$181.59*
Bothell	$5.90	$8.45	$11.77
Kent	$5.95	$7.15	$9.13
Kirkland	$12.91	$18.66	$30.99
Redmond	$14.97	$19.76	$29.84
Renton	$7.32	$9.42	$13.44

Commercial Lease Rates, 2010 Q1

Type	Office Class A	Office Class B	Restaurant Retail
Kirkland	$28.42	$24.12	$16.88
Bellevue CBD	$33.89	$33.77	$28.74
Bellevue (Bel-Red)	$27.46	$23.74	$23.26
Bothell	$22.59	$22.05	$20.15
Kent	$21.61	$20.88	$23.10
Redmond	$24.58	$24.47	$29.53
Renton	$22.30	$20.51	$20.28

Office and Retail Vacancy Rates

	Office			Retail		
City	2003, Q4	2005, Q4	2010, Q1	2003, Q4	2005, H2	2009, Q4
Kirkland	9.3%	4.4%	30.6%	8.6%	0.8%	22.2%
Bellevue CBD	20.8%	9.1%	17.0%	1.5%	11.1%	4.4%
Bellevue (Non-CBD)*	10.1%	9.8%	11.1%	12.8%	2.9%	10.4%
Bothell	-	-	21.4%	0.9%	1.4%	4.6%
Kent	22.9%	24.5%	29.1%	1.9%	2.0%	7.5%
Redmond	11.6%	11.0%	25.7%	4.6%	0.3%	3.7%
Renton	23.6%	30.9%	14.0%	1.2%	0.9%	6.6%

*Bellevue office figures are for the Bel-Red corridor

DEVELOPMENT PERSPECTIVE

Representative Development Types

Type	Acres	GFA	Est. Construction Cost
Large Office Building	2.50	270,000	$47,250,000
Medium Office Building	0.75	80,000	$9,200,000
Big Box Retail	6.50	100,000	$7,000,000
Strip Retail	2.00	45,000	$3,150,000
Mixed Use Development	0.50	120,000	$19,800,000

Summary of Findings

- Land costs are the biggest portion of locally-variable costs
- Kirkland's permit and impact fees are on the higher end of the comparison
- Locally-variable costs are a relatively small share of total project costs
- Costs tend to vary according to the underlying value of a location
- While local tax and fee policies might have some impact on the margin, the impact of these fees on the total cost of development is relatively small

Estimates of Locally Variable Costs by Jurisdiction

Development Type	Kirkland	Bellevue	Bothell	Kent	Redmond	Renton
Large Office Buildings	**$6,036,000**	**$5,652,000**	**$3,610,000**	**$1,394,000**	**$8,078,000**	**$2,212,000**
% of Project Cost	**11.3%**	**10.7%**	**7.1%**	**2.9%**	**14.6%**	**4.5%**
Impact Fees	$1,998,000	$923,000	$1,958,000	NA	$4,357,000	$363,000
Permit Fees	$664,000	$545,000	$371,000	$400,000	$472,000	$385,000
Land Cost	$3,374,000	$4,183,000	$1,281,000	$994,000	$3,250,000	$1,464,000
Medium Office Building	**$1,751,000**	**$1,650,000**	**$1,042,000**	**$378,000**	**$2,624,000**	**$634,000**
% of Project Cost	**16.0%**	**15.2%**	**10.2%**	**3.9%**	**22.2%**	**6.4%**
Impact Fees	$592,000	$274,000	$580,000	NA	$1,528,000	$108,000
Permit Fees	$147,000	$122,000	$77,000	$80,000	$121,000	$87,000
Land Cost	$1,012,000	$1,255,000	$384,000	$298,000	$975,000	$439,000
Big Box Retail	**$9,681,000**	**$11,245,000**	**$4,100,000**	**$2,645,000**	**$9,898,000**	**$4,320,000**
% of Project Cost	**58.0%**	**61.6%**	**36.9%**	**27.4%**	**58.6%**	**38.2%**
Impact Fees	$805,000	$294,000	$707,000	NA	$1,362,000	$450,000
Permit Fees	$103,000	$76,000	$62,000	$60,000	$86,000	$64,000
Land Cost	$8,773,000	$10,875,000	$3,331,000	$2,585,000	$8,449,000	$3,806,000
Strip Retail	**$2,953,000**	**$3,528,000**	**$1,379,000**	**$823,000**	**$3,214,000**	**$1,373,000**
% of Project Cost	**48.4%**	**52.8%**	**30.4%**	**20.7%**	**50.5%**	**30.4%**
Impact Fees	$202,000	$123,000	$324,000	NA	$572,000	$168,000
Permit Fees	$52,000	$58,000	$30,000	$28,000	$43,000	$34,000
Land Cost	$2,699,000	$3,346,000	$1,025,000	$795,000	$2,600,000	$1,171,000
Mixed Use Development	**$1,471,000**	**$1,166,000**	**$839,000**	**$700,000**	**$1,749,000**	**$651,000**
% of Project Cost	**6.9%**	**5.6%**	**4.1%**	**3.4%**	**8.1%**	**3.2%**
Impact Fees	$546,000	$129,000	$425,000	$332,000	$910,000	$188,000
Permit Fees	$251,000	$201,000	$158,000	$169,000	$190,000	$170,000
Land Cost	$675,000	$837,000	$256,000	$199,000	$650,000	$293,000

Relationship of Land Costs and Tax and Fee Policies. Land values likely capture any meaningful distinctions among local tax and fee impacts. As a result, it is worth noting that the low impact fee environment in Kent and Renton may reflect insufficient market value to support impact fees rather than fewer infrastructure needs or a particular "developer-friendly" approach.

BUSINESS OPERATOR PERSPECTIVE

Representative Business Types

Business Type	GFA	Employees	Gross Revenues
Large Office	45,000	150	$16,732,204
Medium Office	13,200	44	$6,733,398
Restaurant	17,100	57	$3,557,002
Big Box	100,000	165	$58,112,725

Summary of Findings

- As with the Development Perspective, real estate costs are the largest portion of locally-variable costs
- The City of Kirkland tax burden is a relatively small share of the total tax burden, though can be more visible
- The degree to which local tax burden is meaningful to a location decision will eventually be reflected in lease rates
- Kirkland's business taxes have a disproprotionate effect depending on type of business:
  - A relatively small factor for high value-added businesses
  - Larger impact on those with lower revenues per employee

Estimates of Locally Variable Costs by Jurisdiction

Business Type	Kirkland	Bellevue	Bothell	Kent	Redmond
Large Office	**$1,778,000**	**$1,735,000**	**$1,508,500**	**$1,472,600**	**$1,601,000**
% of Gross Rev.	**10.6%**	**10.4%**	**9.0%**	**8.8%**	**9.6%**
Annual Rent	$1,279,000	$1,236,000	$1,017,000	$972,000	$1,106,000
State & Regional Taxes	$447,000	$443,000	$456,000	$458,000	$447,000
Local Taxes	$52,000	$56,000	$35,500	$42,600	$48,000
Property	*$8,500*	*$7,000*	*$9,500*	*$16,000*	*$10,500*
Sales	*$9,000*	*$9,000*	*$9,000*	*$9,000*	*$9,000*
Utility	*$19,500*	*$15,000*	*$16,000*	*$17,500*	*$15,000*
Business	*$15,000*	*$25,000*	*$1,000*	*$100*	*$13,500*
Medium Office	**$554,000**	**$544,000**	**$475,500**	**$464,100**	**$502,000**
% of Gross Rev.	**8.2%**	**8.1%**	**7.1%**	**6.9%**	**7.5%**
Annual Rent	$375,000	$362,000	$298,000	$285,000	$324,000
State & Regional Taxes	$164,000	$163,000	$167,000	$167,000	$164,000
Local Taxes	$15,000	$19,000	$10,500	$12,100	$14,000
Property	*$2,500*	*$2,000*	*$3,000*	*$4,500*	*$3,000*
Sales	*$2,500*	*$2,500*	*$2,500*	*$2,500*	*$2,500*
Utility	*$5,500*	*$4,500*	*$4,500*	*$5,000*	*$4,500*
Business	*$4,500*	*$10,000*	*$500*	*$100*	*$4,000*
Restaurant	**$358,500**	**$462,500**	**$409,500**	**$463,100**	**$570,500**
% of Gross Rev.	**10.1%**	**13.0%**	**11.5%**	**13.0%**	**16.0%**
Annual Rent	$289,000	$398,000	$345,000	$395,000	$505,000
State & Regional Taxes	$51,000	$50,000	$54,000	$55,000	$51,000
Local Taxes	$18,500	$14,500	$10,500	$13,100	$14,500
Property	*$3,000*	*$2,500*	*$3,000*	*$5,000*	*$3,500*
Sales	*$1,500*	*$1,500*	*$1,500*	*$1,500*	*$1,500*
Utility	*$8,000*	*$5,000*	*$5,500*	*$6,500*	*$4,500*
Business	*$6,000*	*$5,500*	*$500*	*$100*	*$5,000*
Big Box	**$2,165,000**	**$2,847,000**	**$2,471,000**	**$2,783,100**	**$3,413,500**
% of Gross Rev.	**3.7%**	**4.9%**	**4.3%**	**4.8%**	**5.9%**
Annual Rent	$1,688,000	$2,326,000	$2,015,000	$2,310,000	$2,953,000
State & Regional Taxes	$398,000	$393,000	$408,000	$411,000	$398,000
Local Taxes	$79,000	$128,000	$48,000	$62,100	$62,500
Property	*$10,500*	*$8,500*	*$11,000*	*$19,000*	*$12,500*
Sales	*$6,000*	*$6,000*	*$6,000*	*$6,000*	*$6,000*
Utility	*$46,000*	*$26,500*	*$30,000*	*$37,000*	*$29,000*
Business	*$16,500*	*$87,000*	*$1,000*	*$100*	*$15,000*

POLICY CONSIDERATIONS

Overall Assessment

- City's ability to use tax and fee policies to affect business decisions is likely to be limited, since these are relatively small components of overall cost
- Changes in tax and fee policies designed to improve competitiveness must consider how lower City revenues might affect the broader attractiveness of Kirkland for businesses and development
- Given the current economic conditions, any efforts to focus on competitiveness should target keeping existing businesses and filling existing vacant spaces

Development Perspective

- Predictability and timeliness of development is generally more important than absolute costs of permitting or impact fees.
- Currently, impact fees on changes in use for existing vacant properties may be an unnecessary hurdle
- With high vacancy rates, there is additional capacity on the local roadway system
- Consider treating additions to building capacity differently from changes to existing commercial inventory
- One option might be to suspend impact fees for activity related to filling existing commercial spaces until vacancy rates return to "normal" levels

Business Owner/Operator Perspective

- While local tax and fee policies are a small portion of the cost of doing business in the City, the "head tax" is highly visible
- For many businesses, the business taxes are not likely to be a significant deterrent to locating in Kirkland
- The exceptions may be businesses with lower gross business income per employee
- Possibly consider options for refining business taxes to account for impact on these businesses
- Challenges would be to avoid opening up the discussion too broadly and accounting for the revenue impacts of any changes

ATTACHMENT

Technical Report

COMPETITIVENESS ASSESSMENT:
COST OF DOING BUSINESS IN KIRKLAND

To inform discussions about the City's fiscal policies and its overall financial position, the City of Kirkland retained BERK in 2008 to perform a Tax Burden Study. The study built upon work performed in Kirkland's 2001 Tax Burden Analysis, adopting and extending much of the 2001 framework. In particular the analysis presented findings on:

- Tax burdens borne by a range of representative taxpayers in the city;
- Shifts in tax burdens over time (1996-2007);
- How current tax burdens in Kirkland compared to those in peer jurisdictions; and
- Overall contributions made by Kirkland's households and businesses (viewed as groups) to the city's tax revenue streams.

In the budgeting process that followed the Tax Burden Study, City policy makers took many actions to curtail expenditures in the biennial budget and they took a number of actions to augment revenues. Among the most high-profile of these revenue actions was the restructuring of the City's business tax to a "head tax."

At this time, the Economic Development Department has a need for some additional follow-up analysis to supplement the 2008 study. In particular, the Department is interested in addressing broader questions relating to the City's local competitiveness and the possible role of tax and fee policies on the City's ability to attract and retain commercial businesses including the City's ability to compete for new commercial development that would grow the local tax base.

To inform this broader discussion, BERK was retained to conduct a competitiveness assessment that would build on the tax burden analysis, which is one component of local competitiveness, by looking at how the City's tax and fee policies might be affecting the City's ability to remain competitive among its local peer communities.

There are two perspectives that the City has an interest in when examining the issue of local competitiveness in attracting business activity. The first is a development perspective, with a particular focus on the costs associated with doing business <u>with</u> the City. The other perspective is the business operator perspective, with a focus on the costs of doing business <u>in</u> the City of Kirkland. These perspectives are explained below:

1. **Cost of Doing Business <u>with</u> Kirkland (Development Perspective).** The analysis of doing business with the City of Kirkland addresses how costs associated with permitting and impact fees compare with both other cities and with overall costs of development. This is a key element of competitiveness as developers look to limit their costs and risks while seeking development opportunities within the broader eastside marketplace. For similar projects, land costs and the costs of doing business with the host jurisdiction are the key locally-variable costs, while construction costs tend to be less variable site-to-site (excepting site prep/critical area issues).
2. **Cost of Doing Business <u>in</u> Kirkland (Business Operator Perspective).** The analysis of the business operator perspective considers the relative cost of doing business in the City of Kirkland. Beyond tax burdens, the analysis will also consider the lease rates, which is the other principal locally-variable business cost.

Ultimately, businesses do not base their location decisions purely on an assessment of these locally-variable costs. Rather, businesses make siting decisions by balancing costs against locational benefits, particularly with respect to the things they need from their place of business:

- Access to markets and customers; and,
- Access to the factors of production:
    - Access to and ability to attract the appropriate labor force;
    - Access to non-labor production inputs/supplies;
    - Access to capital; and,
    - Availability of entrepreneurial initiative

As a result, a key part of this assessment is to put the locally-variable cost comparison data in a market context, since the real question is not whether costs are higher but whether costs can be justified based on perceived value. For example, we can be certain that the cost of doing business will be higher in Bellevue than it is in communities in south King County. Yet, Bellevue has been much more successful at achieving employment growth than have the smaller communities in south King County. Clearly, businesses are willing to pay a premium for a location based on the value of that location in relation to the success of their enterprise, whether the enterprise is real estate development or operating a business in an office or retail space.

To explore these issues, this assessment focuses on estimating the location-driven costs of doing business for five representative development types (development perspective) and four representative businesses (business operator perspective). The representative businesses are a subset of the ten representative commercial taxpayers that were examined as part of the 2008 Tax Burden Study, focusing on operators which might best represent the broadest perspective for all business types.

Exhibit 1
Representative Developments and Businesses

Representative Developments	Representative Businesses
Large Office	Large Office
Medium Office	Medium Office
Big Box Retail	Big Box Retailer
Neighborhood (Strip) Retail	Restaurant
Mixed Use (residential/retail)	

The analysis examines the locally-variable costs with costs that these developments and businesses would face if they were located in each of the peer cities examined in the 2008 Tax Burden study:

- Bellevue
- Bothell (KC Portion)
- Kent
- Redmond
- Renton

Since this analysis is focused primarily on local competitiveness for commercial enterprises, the comparisons focus on the other cities in the 2008 tax burden study and do not include unincorporated parts of King County. This decision was made based on two factors: (1) most of the competitive

commercial areas are located in cities; and, (2) there are data availability issues that limit the ability to look at isolated areas within the broader unincorporated parts of King County.

Summary of Findings

Exhibit 2 summarizes the results of the competitive assessment for both the development perspective and the business owner perspective. The table shows how locally-variable costs relate to total project cost, in the case of the new development scenario or gross business income in the business owner perspective. For each perspective, the locally-variable costs are the major costs that will vary based on choice of location and include real estate costs and costs associated with local taxes and fees. The summary table illustrates the range of impacts using the lowest and highest value projects and businesses to illustrate the overall impact of local tax and fee policy on city competitiveness. The assessments are described in greater detail later in the report.

Exhibit 2
Summary of Key Factors in Local Competitiveness (in $1,000s)

	Kirkland		Bellevue		Bothell		Kent		Redmond		Renton	
	Low Value	High Value	Low Value	High Value	Low Value	High Value	Low Value	High Value	Low Value	High Value	Low Value	High Value
DEVELOPMENT PERSPECTIVE												
Total Project Cost	**$6,103**	**$53,286**	**$6,678**	**$52,902**	**$4,529**	**$50,860**	**$3,973**	**$48,644**	**$6,364**	**$55,328**	**$4,523**	**$49,462**
Local Variable Costs	$2,953	$6,036	$3,528	$5,611	$1,379	$3,446	$823	$1,272	$3,214	$8,388	$1,373	$2,053
Impact Fees	$202	$1,998	$123	$917	$324	$1,869	NA	NA	$572	$4,524	$168	$337
Permit Fees	$52	$664	$58	$541	$30	$354	$28	$365	$43	$490	$34	$357
Land Cost	$2,699	$3,374	$3,346	$4,153	$1,025	$1,223	$795	$907	$2,600	$3,374	$1,171	$1,359
Local Variable Costs	48.4%	11.3%	52.8%	10.6%	30.4%	6.8%	20.7%	2.6%	50.5%	15.2%	30.4%	4.2%
Impact Fees	3.3%	3.7%	1.8%	1.7%	7.1%	3.7%	NA	NA	9.0%	8.2%	3.7%	0.7%
Permit Fees	0.9%	1.2%	0.9%	1.0%	0.7%	0.7%	0.7%	0.8%	0.7%	0.9%	0.8%	0.7%
Land Cost	44.2%	6.3%	50.1%	7.8%	22.6%	2.4%	20.0%	1.9%	40.8%	6.1%	25.9%	2.7%
BUSINESS OWNER PERSPECTIVE												
Gross Revenue	**$3,557**	**$16,732**	**$3,557**	**$16,732**	**$3,557**	**$16,732**	**$3,557**	**$16,732**	**$3,557**	**$16,732**	**$3,557**	**$16,732**
Local Variable Costs	$307	$1,331	$412	$1,292	$355	$1,052	$408	$1,015	$520	$1,154	$363	$1,056
Local Taxes	$19	$53	$14	$56	$11	$36	$13	$43	$15	$48	$17	$53
Rent	$289	$1,279	$398	$1,236	$345	$1,017	$395	$972	$505	$1,106	$347	$1,004
Local Variable Costs	8.6%	8.0%	11.6%	7.7%	10.0%	6.3%	11.5%	6.1%	14.6%	6.9%	10.2%	6.3%
Local Taxes	0.5%	0.3%	0.4%	0.3%	0.3%	0.2%	0.4%	0.3%	0.4%	0.3%	0.5%	0.3%
Rent	8.1%	7.6%	11.2%	7.4%	9.7%	6.1%	11.1%	5.8%	14.2%	6.6%	9.7%	6.0%

Source: Rider Levett Bucknall, 2010; BERK, 2010

Overall there were several key findings that have emerged from the competitive assessments,

- The largest share of locally-variable costs are derived from the relative values placed on different locations (i.e. rent costs or land costs).
- The portion of locally-variable costs that are attributable to tax and fee policies is a relatively small share of total locally-variable costs and of the total size of a given development project or business.
- The City of Kirkland is among the higher cost places to do business due to both market factors and tax and policy decisions.
- There is a general correlation between cities that have higher land values and lease rates and higher local costs associated with tax and fee policy.

- Given the relatively small share of total development and business costs that are attributable to local tax and fee policies, it is unclear how much impact changes in these policies might have on local competitiveness.
- The more significant factors affecting local competitiveness are those that increase demand for real estate, since these lead to increases in the price that businesses are prepared to pay to secure a location within a particular commercial district and generate the underlying economic value that supports the local tax and fee policies.
- It is important to not lose sight of the fact that the costs attributable to local tax and fee policies do provide value to developers and business owners, which can contribute to supporting the overall attractiveness of the City and thus the rents that can be achieved, for example:
    - Impact fees fund necessary capital improvements; and
    - Local taxes fund public services like public safety and amenities such as waterfront parks.

Development Perspective. Development profitability is a function of the income producing capacity of the project and the costs of developing the project. As a result, local government actions that are designed to influence development decisions must either address the cost (including development risk factors) or the market value of the project. The assessment of local competitiveness compares the locally-variable costs to the total cost of development and looks at how much of the locally-variable costs are attributable to local jurisdictions' tax and fee policies. Overall findings from this assessment include:

- Land costs are the primary driver of locally-variable costs. As development projects increase in value and density, land costs become smaller share of total development costs. Higher land values are a reflection of how the market values the commercial opportunities in a given community and correlate with higher lease rates that individual businesses are willing to pay to operate in these commercial centers.
    - Kirkland's land values ($31/SF) for commercially-zoned property are similar to Redmond ($30/SF) and generally lower than Bellevue ($38/SF outside of CBD, $182/SF in CBD) but substantially higher than Kent ($9/SF), Renton ($13/SF) and Bothell ($12/SF).
- City of Kirkland's permit fees appear to be somewhat higher than some of its peer jurisdictions, though the actual dollar value differences may not be material in the context of the overall share of development costs.
- City of Kirkland's impact fees are higher than all of the peer and neighbor jurisdictions except for Redmond. The fees are substantially higher than the lower land value communities of Kent and Renton and comparable to Bothell.
- While local tax and fee policies might have some impact on the margin, the impact of these fees on the total cost of development is relatively small, though between impact fees and permit fees, impact fees have the larger impact on locally-variable costs.
- Beyond the cost of acquiring development permits, developers also care very much about the predictability and timeliness of the permit review process. Generally, the most important factor in assessing the impact of working with a jurisdiction on permitting is the predictability of the process. Lack of predictability increases development risk which can correlate to higher development costs (i.e. higher interest rates, higher capital requirements) or higher return requirements which can depress land values.
- Land values likely capture any meaningful distinctions among local tax and fee impacts. As a result it is worth noting that the low impact fee environment in Kent and Renton may reflect insufficient market value to support impact fees rather than fewer infrastructure needs or a

particular "developer-friendly" approach. In contrast, Bellevue with its higher values and somewhat lower impact fees probably does reflect a "developer-friendly" building environment.

Business Owner Perspective. The assessment of local competitiveness from the business operator perspective considers the potential impact of the relative differences in tax burden for selected businesses on the City's ability to attract and retain commercial enterprises.

- As with the development perspective, the most significant locally-variable cost factor is lease costs, which vary widely among the peer and neighbor jurisdictions based on the relative attractiveness of the commercial areas.
    - Overall average lease rates in Kirkland are generally higher than its neighbors for office uses (except Bellevue CBD) and somewhat lower for retail uses. In fact, the average lease rates for retail uses are the lowest among the peer and neighbor jurisdictions
- The local tax burden (the portion that varies by locaton) is a very small portion of overall business operator costs.
- As with the development-related costs, any meaningful difference in local tax policy between jurisdictions that are competing for the same market will be reflected in the lease rates that landlords can achieve.
    - Generally, businesses that are particularly sensitive to certain local taxes will consider the costs as part of their decision, which will drive down what they are willing to pay for rent. For example, a high volume/low margin business might be particularly sensitive to a local B&O tax or a business that is very labor intensive might be particularly sensitive to a local head tax.

Policy Considerations. The key policy considerations that arise from this assessment are related to how City actions might influence the competitiveness of local commercial districts in terms of attracting new development and/or attracting and retaining businesses.

- The tax and fee impacts on the competitiveness situation may be a factor, but it is likely a small factor in locational decisions, as the biggest cost factor in locational decisions are related to the cost and availability of real estate (either land prices or lease rates).
- Further, these tax and fee policies have largely been accounted for by market adjustments to real estate costs – either lease rates or land values or both.
- While it is likely that the impact of tax and fee policies is small from a local competitiveness perspective, a reduction in these costs might produce some benefits on the margin.
- Probably the most significant jurisdictional factor that affects the relative attractiveness of development is the predictability and timeliness of development and not the absolute dollar costs of permitting or impact fees.
    - To put this into perspective, the estimated cost of acquiring the necessary building permits, while not insignificant, would likely equate to approximately 2-4 months of interest costs on construction loans.
    - Strategies designed to promote new development should generally start with addressing predictability and timeliness issues.
- To the extent that a strategy to reduce local tax and fee impacts on development (through reduced impact fees and/or reduced permit fees) had a meaningful impact it would likely either:
    - Provide some incentive to develop for current property owners who could then capitalize on the lower cost of development; or,
    - Increase the price of land as prospective developers bid up the land costs, shifting the benefits of the lower permitting costs to property owners and having minimal impact on the overall incentive to develop.

- It is important not to focus exclusively on the cost side of the equation, since a big part of attracting and retaining businesses is the real and perceived value of locating in the City. In particular, Kirkland benefits from its location on Lake Washington and proximity to major highways, other employment centers, high income neighborhoods and significant cultural, recreational and entertainment opportunities. Efforts to leverage and enhance these characteristics are likely to have as much or greater impact on locational decisions.
    - By looking at the value part of the equation, it becomes important to remember that the costs discussed in this assessment are also revenues to the City that support infrastructure development and local services, which are important parts of the value equation.
- The current economic climate is one where the challenge for local jurisdictions is primarily on the demand side – there are fewer businesses, lower employment levels, lower sales. In considering policy options that might stimulate business activity, the focus should be primarily on strategies to boost sales for existing businesses and reduce vacancies among existing office and retail properties.
    - With vacancies at historic highs, strategies targeting incentives for new development are unlikely to provide much immediate benefit.

The following sections provide a brief discussion of the approach, key assumptions and findings for each element of the study:

1. Cost of doing business with the City of Kirkland (Development Perspective)
2. Cost of doing business in the City of Kirkland (Business Owner Perspective)
3. Market Perspective on Local Competitiveness

Cost of Doing Business <u>with</u> City of Kirkland (Development Perspective)

The development perspective assessment presents an analysis of the key locally-variable costs associated with new development, namely land costs, impact fees and permit fees. For this comparison, representative profiles for different development types were developed and are presented in Exhibit 3, including the building scale and type of project and the estimated construction cost for each development. The mixed use development assumes ground level retail space with five stories of residential units above.

Exhibit 3
Representative Development Types

Type	Acres	GFA	Stories	FAR	Est. Construction Cost
Large Office Building	2.50	270,000	6	2.48	$47,250,000
Medium Office Building	0.75	80,000	3	2.45	$9,200,000
Big Box Retail	6.50	100,000	1	0.35	$7,000,000
Strip Retail	2.00	45,000	1	0.52	$3,150,000
Mixed Use Development	0.50	120,000	6	5.51	$19,800,000

Source: Rider Levett Bucknall, 2010; BERK, 2010

Exhibit 4 presents the estimates of locally variable costs by jurisdiction for each of the representative development types. It is worth noting that this analysis is at a conceptual level and designed to highlight local policy implications. As such the the fee estimates are based on generic development types and

current development fee ordinances. The permit fees in particular reflect the principal permits that would likely be required for a new development and do not fully account for all of the likely permit costs, nor do they capture any costs associated with potential differences in permit review time. Since most jurisdictions seek to recover their permit review costs through permit fees, the fee structures will also depend on the expected level of development activity at any given time and/or the level of staffing that is offered to meet the expected demand.

Exhibit 4

Estimates of Locally-Variable Costs by Jurisdiction

Development Type	Kirkland	Bellevue	Bothell	Kent	Redmond	Renton
Large Office Buildings	**$6,036,000**	**$5,652,000**	**$3,610,000**	**$1,394,000**	**$8,078,000**	**$2,212,000**
Impact Fees	$1,998,000	$923,000	$1,958,000	NA	$4,357,000	$363,000
Permit Fees	$664,000	$545,000	$371,000	$400,000	$472,000	$385,000
Land Cost	$3,374,000	$4,183,000	$1,281,000	$994,000	$3,250,000	$1,464,000
Medium Office Building	**$1,751,000**	**$1,650,000**	**$1,042,000**	**$378,000**	**$2,624,000**	**$634,000**
Impact Fees	$592,000	$274,000	$580,000	NA	$1,528,000	$108,000
Permit Fees	$147,000	$122,000	$77,000	$80,000	$121,000	$87,000
Land Cost	$1,012,000	$1,255,000	$384,000	$298,000	$975,000	$439,000
Big Box Retail	**$9,681,000**	**$11,245,000**	**$4,100,000**	**$2,645,000**	**$9,898,000**	**$4,320,000**
Impact Fees	$805,000	$294,000	$707,000	NA	$1,362,000	$450,000
Permit Fees	$103,000	$76,000	$62,000	$60,000	$86,000	$64,000
Land Cost	$8,773,000	$10,875,000	$3,331,000	$2,585,000	$8,449,000	$3,806,000
Strip Retail	**$2,953,000**	**$3,528,000**	**$1,379,000**	**$823,000**	**$3,214,000**	**$1,373,000**
Impact Fees	$202,000	$123,000	$324,000	NA	$572,000	$168,000
Permit Fees	$52,000	$58,000	$30,000	$28,000	$43,000	$34,000
Land Cost	$2,699,000	$3,346,000	$1,025,000	$795,000	$2,600,000	$1,171,000
Mixed Use Development	**$1,471,000**	**$1,166,000**	**$839,000**	**$700,000**	**$1,721,000**	**$978,000**
Impact Fees	$546,000	$129,000	$425,000	$332,000	$882,000	$515,000
Permit Fees	$251,000	$201,000	$158,000	$169,000	$190,000	$170,000
Land Cost	$675,000	$837,000	$256,000	$199,000	$650,000	$293,000

Source: BERK, 2010

- Land costs are the largest locally-variable cost factor, in some cases by a wide margin. The land costs in this analysis are based on an overall average of land values for commercially-zoned land as estimated by the King County Assessor's Office. While individual sale prices will vary greatly, this estimate provides a reasonable overall measure of the relative value of commercial properties in the peer and neighbor jurisdictions.
- Land costs also already account for any meaningful differential in permit or impact fee costs since buyers would be factoring these cost differentials into what they are willing to pay for a piece of land.
    - For example, while the City of Kent presents developers with significantly lower local costs, both low permit fees and no impact fees, these lower costs are also matched with very low land prices. So another way to think about these low development costs is that the market is not strong enough to support an impact fee program. Thus, the lack of impact fees on development is actually a sign of a weak commercial market (in terms of valuations) as opposed to a significant competitive advantage.
- Impact fees vary, both in terms of the particular impact fee rates but also in which fees, in any, are charged.

  - For commercial development the key is transportation impact fees where Kirkland is on par with Bothell, but substantially lower than Redmond and substantially higher than Bellevue and Renton. Kent does not assess impact fees on commercial development.
  - For the mixed use projects, residential impact fees play into the equation. In this case, Kirkland's parks fee is on par with Redmond.
- Overall, there is not a significant difference in total permit fees amongst the peer citites. Both Kirkland and Bellevue have fee totals higher than the other peer cities with Kirkland's being the highest for all of the development types with the exception of strip retail.
  - The primary reason for higher fees in Kirkland are that the City's building, mechanical and electrical permits are all on the higher end compared to those of the peer cities**.**
- Permit fees represent a small share of a projects overall cost. In Kirkland, they are no more than 1.3% of a development projects overall cost. For Bellevue, Bothell, Kent, and Renton they are all around 1.0% or less.

Permit fees. Building fees for Kirkland and the five other peer cities – Bellevue, Bothell, Kent, Redmond, and Renton – were gathered from each of the cities' municipal code and related documents available on their websites. Building fees required for commercial development vary from city to city, however all of the cities reviewed in this assessment charged at least a building permit fee and plan review fee**.** In addition to these two fees, a number of the cities charged other types of fees including:

- Design Review Fees
- Fire Plan Review Fees
- Engineering Plan Review Fees
- Mechanical Fees
- Electrical Fees

All of the cities reviewed calculate these fees in a similar method. For example, the building permit fees have a base fee scaled on the total value of the development. Developments valued above an established threshold pay an additional fee amount based on the value of the remainder of the development above that threshold. Exhibit 5 summarizes the fee rates for these representative permits for each of the peer and neighbor jurisdictions.

Exhibit 5
Representative Permit Rates by Jurisdiction, 2010

Development Permit Rates	Kirkland	Bellevue	Bothell	Kent	Redmond	Renton
Building Permit Fee	$3,430 + $5.04 each $1,000 over $500k	<$5M: $7,836 + $4.35 each $1,000 over $500k >$5M: 25,236 + $3.82 each $1,000 over $5M	$6,730 + $4.50 each $1,000 over $1M	$6,042 + $5.10 each $1,000 over $1M	$4,109 + 0.365% of value over $1M	$6,615 + $4.35 each $1,000 over $1M
Plan Review Fee	65% of building permit fee	65% of building permit fee	65% of building permit fee	65% of building permit fee	$2,027 + 0.237% of value over $1M	65% of building permit fee
Design Review Fee	$1,427 + $4,371 + $0.20/SF new GFA + $201/res. Unit			$588		
Fire Plan Check Fee		$124/hour	$0.06/SF		$2,064	
Engineering Plan Check Fee					$0.16/SF (commercial) or $164.90/Unit (residential)	
Mechanical Fee	$1,710 + $14.86 each $1,000 over $100k*	$2,098 + $15.40 each $1,000 over $100k*	Charge per fixture	Charge per fixture	<$1M: $89.31 + $19.63 each $1,000 over $1,000 $1M-$2M: $19,712 + $9.87 each $1,000 over $1M >$2M: $29,580 + $5.95 each $1,000 over $2M	Charge per fixture
Electrical Fee	$1,433 + $8.70 each $1,000 over $100k*	$1,806 + $11.49 each $1,000 over $100k*	-	-	$250k-$1M: $5,061 + 1.3% of cost over $250k >$1M: $15,632 + 0.7% of cost over $1M	$250k-$1M: $3,573 + 0.8% of value* >$1M: $11,573 + 0.4% of value*
Technology Surcharge	-	-	-	-	3% of building fee	-

Source: City of Bellevue; City of Bothell; City of Kent; City of Kirkland; City of Redmond; City of Renton; BERK, 2010

Impact Fees. Among the studied peer locations and development types, the City of Kirkland's impact fees generally fall into the middle of the range. For the example developments analyzed in this assessment, Kirkland's impact fees are consistently and significantly lower than those charged by Redmond, and consistently higher than Bellevue and Renton. The City of Bothell is relatively similar to Kirkland. The summary of these impact fees for example developments is shown in Exhibit 6.

There is some variation in Kirkland's competitive position based on whether or not the development includes residential properties. The City of Kirkland is less competitive for developments with residential units, such as a mixed-use development, due to the City's park impact fees. The total fee charged on the example mixed-use development is higher for Kirkland than for all other cities except Redmond.

For developments with only commercial properties, Kirkland is consistently in the middle of the impact fee range. Kirkland charges only traffic impact fees on these developments, as do Bellevue and Bothell. Renton also charges fire impact fees, and Redmond charges both fire and park fees. Redmond consistently has the highest total impact fee for all types of development.

Exhibit 6
Summary of Impact Fees Paid by Development Type and Jurisdiction

Type of Development	Kirkland		Bellevue		Bothell		Kent		Redmond		Renton	
	Rate	Units	Rate	Units	Rate	Units	Rate	Units	Rate	Units	Rate	Units
Large Office Buildings												
Traffic[1]	$7.40	SF/GFA	$3.42	SF/GFA	$7.04	SF/GFA	NA	NA	$14.97	SF/GFA	$0.83	SF/GFA
Fire	-	-	-	-	-	-	-	-	$144	1,000 GFA	$0.52	per SF
Parks	-	-	-	-	-	-	-	-	$1,022	1,000 GFA	-	-
Schools	-	-	-	-	-	-	-	-	-	-	-	-
Medium Office Building												
Traffic	$7.40	SF/GFA	$3.42	SF/GFA	$7.04	SF/GFA	NA	NA	$17.93	SF/GFA	$0.83	SF/GFA
Fire	-	-	-	-	-	-	-	-	$144	1,000 GFA	$0.52	per SF
Parks	-	-	-	-	-	-	-	-	$1,022	1,000 GFA	-	-
Schools	-	-	-	-	-	-	-	-	-	-	-	-
Big Box Retail												
Traffic	$8.05	SF/GFA	$2.94	SF/GFA	$6.85	SF/GFA	NA	NA	$13.01	SF/GFA	$8.86	SF/GFA
Fire	-	-	-	-	-	-	-	-	$166.00	1,000 GFA	$0.52	per SF
Parks	-	-	-	-	-	-	-	-	$448.00	1,000 GFA	-	-
Schools	-	-	-	-	-	-	-	-	-	-	-	-
Strip Retail												
Traffic	$4.48	SF/GFA	$2.74	SF/GFA	$6.95	SF/GFA	NA	NA	$12.09	SF/GFA	$3.22	SF/GFA
Fire	-	-	-	-	-	-	-	-	$166	1,000 GFA	$0.52	per SF
Parks	-	-	-	-	-	-	-	-	$448	1,000 GFA	-	-
Schools	-	-	-	-	-	-	-	-	-	-	-	-
Mixed Use Development[2]												
Traffic	$4.48	SF/GFA	$1.90	SF/GFA	$6.95	SF/GFA	NA	NA	$9.34	SF/GFA	$5.19	SF/GFA
Fire	-	-	-	-	-	-	-	-	$174	per Unit	$388	per Unit
Parks	$2,515	per Unit	-	-	$762	per Unit	-	-	$2,414	per Unit	$355	per Unit
Schools[3]	-	-	-	-	-	-	$3,322	per Unit	$280	per Unit	-	-

[1] Bothell also has a 3% admin. fee and a $1633 traffic mitigation fee which varies on the number of trips/hr. Renton traffic rates are $75 per additional trip. Converted to dollars per square foot for comparison.

[2] Park and School fee rates are shown for residential portion only; Traffice fee rates are for commercial portion only.

[3] Kent School District Fees applied for Kent; Lake Washington School District Fees applied for Redmond

GFA: Gross Floor Area

Source: City of Kirkland, City of Bellevue, City of Bothell, City of Kent, City of Redmond, City of Renton, BERK, 2010.

Notes: The City of Kent only charges traffic impact fees if the proposed development's traffic impact would cause the affected routes to no longer be in GMA compliance.

Cost of Doing Business in Kirkland (Business Operator Perspective)

The local tax assessment summarizes the total local tax burden for four representative businesses used in the 2008 Kirkland Tax Burden Study as part of determining the relative cost of doing business in the City of Kirkland. Exhibit 7 gives an overview of the four representative businesses used in the updated tax burden assessment.

Exhibit 7

Representative Business Profiles

Business Type	GFA	Employees	Gross Revenues
Large Office	45,000	150	$16,732,204
Medium Office	13,200	44	$6,733,398
Restaurant	17,100	57	$3,557,002
Big Box	100,000	165	$58,112,725

Source: BERK, 2010

Exhibit 8

Comparative Annual Taxes, 2010

Business Type	Kirkland	Bellevue	Bothell	Kent	Redmond	Renton
Large Office	**$500,000**	**$504,000**	**$483,000**	**$490,000**	**$496,000**	**$500,000**
State & Regional	$448,000	$448,000	$447,500	$447,400	$448,000	$447,000
Local	$52,000	$56,000	$35,500	$42,600	$48,000	$53,000
Property	*$8,500*	*$7,000*	*$9,500*	*$16,000*	*$10,500*	*$18,500*
Sales	*$9,000*	*$9,000*	*$9,000*	*$9,000*	*$9,000*	*$9,000*
Utility	*$19,500*	*$15,000*	*$16,000*	*$17,500*	*$15,000*	*$17,000*
Business	*$15,000*	*$25,000*	*$1,000*	*$100*	*$13,500*	*$8,500*
Medium Office	**$180,000**	**$183,000**	**$175,000**	**$177,000**	**$178,000**	**$180,000**
State & Regional	$165,000	$164,000	$164,500	$164,900	$164,000	$164,500
Local	$15,000	$19,000	$10,500	$12,100	$14,000	$15,500
Property	*$2,500*	*$2,000*	*$3,000*	*$4,500*	*$3,000*	*$5,500*
Sales	*$2,500*	*$2,500*	*$2,500*	*$2,500*	*$2,500*	*$2,500*
Utility	*$5,500*	*$4,500*	*$4,500*	*$5,000*	*$4,500*	*$5,000*
Business	*$4,500*	*$10,000*	*$500*	*$100*	*$4,000*	*$2,500*
Restaurant	**$70,000**	**$66,000**	**$62,000**	**$65,000**	**$66,000**	**$68,000**
State & Regional	$51,500	$51,500	$51,500	$51,900	$51,500	$51,500
Local	$18,500	$14,500	$10,500	$13,100	$14,500	$16,500
Property	*$3,000*	*$2,500*	*$3,000*	*$5,000*	*$3,500*	*$6,000*
Sales	*$1,500*	*$1,500*	*$1,500*	*$1,500*	*$1,500*	*$1,500*
Utility	*$8,000*	*$5,000*	*$5,500*	*$6,500*	*$4,500*	*$6,000*
Business	*$6,000*	*$5,500*	*$500*	*$100*	*$5,000*	*$3,000*
Big Box	**$477,000**	**$526,000**	**$447,000**	**$460,000**	**$461,000**	**$468,000**
State & Regional	$398,000	$398,000	$399,000	$397,900	$398,500	$398,500
Local	$79,000	$128,000	$48,000	$62,100	$62,500	$69,500
Property	*$10,500*	*$8,500*	*$11,000*	*$19,000*	*$12,500*	*$21,500*
Sales	*$6,000*	*$6,000*	*$6,000*	*$6,000*	*$6,000*	*$6,000*
Utility	*$46,000*	*$26,500*	*$30,000*	*$37,000*	*$29,000*	*$33,000*
Business	*$16,500*	*$87,000*	*$1,000*	*$100*	*$15,000*	*$9,000*

Source: City of Kirkland, City of Bellevue, City of Bothell, City of Kent, City of Redmond, City of Renton, King County, BERK, 2010

BERK used the same approach for this assessment as in the 2008 study. Assumptions about the number of employees, floor area, retail and utility purchase levels, and utility tax distribution all stayed the same. Changes include updating tax rates, inflating business retail and utility purchases to 2010 dollars, and updating business gross revenue estimates. One of the most notable changes since the 2008 study is that the City of Kirkland has restructured it business tax to a “head tax”. Local taxes evaluated for each

representative business includes the major sources of local funding including property, sales, utility, and business taxes and are summarized in Exhibit 8.

Overall, Bellevue has the highest taxes for three of the four representative businesses. Kirkland is second highest except for the restaurant example, where it has the highest local taxes. Overall**,** local taxes are relatively small as a percentage of each representative business' annual gross revenue**.** Exhibit 9 shows the percent of gross revenue that local taxes represent. Taxes for each of the representative business are less than 0.50% of gross revenue in almost all of the peer cities. Taxes for the representative restaurant in Kirkland have the largest percentage, which is 0.52%.

The difference in taxes between peer cities is not that large, either. The representative restaurant in Kirkland would pay almost $8,000 more in taxes annually than the same restaurant in Bothell, the peer city with the lowest taxes for the restaurant. This difference is relatively small compared to the restaurants annual gross revenues of $3.5 million. The additional $8,000 the restaurant pays in taxes is estimated to be approximately 0.2% of its gross revenue.

Exhibit 9

Annual State and Local Taxes as a Percent of Annual Gross Revenue, 2010

	Large Office		Medium Office		Restaurant		Big Box	
City	Local	Total	Local	Total	Local	Total	Local	Total
Kirkland	0.31%	2.99%	0.23%	2.67%	0.52%	1.96%	0.14%	0.82%
Bellevue	0.34%	3.01%	0.29%	2.72%	0.40%	1.84%	0.22%	0.91%
Bothell	0.21%	2.89%	0.16%	2.60%	0.30%	1.75%	0.08%	0.77%
Kent	0.25%	2.93%	0.19%	2.62%	0.38%	1.82%	0.11%	0.79%
Redmond	0.29%	2.96%	0.21%	2.65%	0.42%	1.86%	0.11%	0.79%
Renton	0.31%	2.99%	0.23%	2.67%	0.47%	1.91%	0.12%	0.81%

Source: City of Kirkland, City of Bellevue, City of Bothell, City of Kent, City of Redmond, City of Renton, King County, BERK, 2010

Locally-variable taxes are a small part of the total state and local tax burden for businesses and can be difficult for businesses to separate which taxes are local and which are accruing to other jurisdictions, such as with the sales or property taxes. The exception however is when there is a locally levied and collected tax, such as a local B&O or a local employment tax. In this case it is clear, not only who is levying the tax, but also may lead to a perception that this tax is an "extra" tax. This makes it particularly difficult for a business owner to assess the true local tax differentials. For example, while Kent does not have a B&O tax or an employment tax, the City has higher property taxes which are not as visible and would tend to overstate the difference in local tax burdens between Kent and cities that do have employment taxes.

To the extent that they are meaningful to businesses in their locational decisions, variations in locally-variable tax burdens are likely already be reflected in local lease rate differentials. Generally, business owners are aware of the more meaningful local tax differentials, such as which cities have a local B&O tax and which do not. This knowledge gets incorporated into leasing decisions and, on the margins, will likely push down lease prices to account for these other costs of locating in a particular community.

Market Perspective

It is useful to look at the broader market perspective to see how the market views the relative attractiveness of local commercial districts. It is easy to be too focused on the relatively small differences in costs associated with variations in local tax and fee policies. The best market indicators are those that highlight the value that is placed on being in a particular location, namely the price that

the market is willing to pay to acquire land or secure a lease in one commercial area versus another. By this measure, Kirkland is viewed as a relatively high value location where the market is willing to pay more than some of the peer and neighbor jurisdictions.

Land costs. Land cost is not a development cost that policy-makers have direct control over as with impact and permit fees, but it is a locally based cost for developers that influence the location decisions for different development types. Land costs reflect the market fundamentals and desirability of that location based on the rents that one can expect to get at that location. High land values represent a desirable area with strong demand.

This assessment evaluated the difference in the average value per square foot of land that a developer would likely pay in each of the six peer cities. Because the value reflects the expected rents from that location, parcels were analyzed based on their zoning and thus the development potential for the five development types – large office building, medium office building, big box retail, strip retail, and a mixed use building. The total assessed land value and square footage for the selected parcels was summed by the develop type the zoning allowed and used to calculate an average value per square foot in each city.

Bellevue, Kirkland, and Redmond have the highest average land values of all the peer cities. Kent and Renton in south King County and Bothell to the north have the lowest average land values. Exhibit 10 lists the average land value for each city.

Exhibit 10

Average Land Value per Square Foot (Commercial Zoning)

City	2003	2007	2010
Bellevue (Outside of Downtown)	$13.93	$21.08	$38.41
Downtown Bellevue	*$70.32*	*$86.92*	*$181.59*
Bothell	$5.90	$8.45	$11.77
Kent	$5.95	$7.15	$9.13
Kirkland	$12.91	$18.66	$30.99
Redmond	$14.97	$19.76	$29.84
Renton	$7.32	$9.42	$13.44

Source: King County, 2010; BERK, 2010

Overall, land acquisition in Kirkland will likely be more expensive for a developer compared the other peer cities with the exception of Bellevue and possibly Redmond. Higher land costs are not necessarily a negative. They indicate that Kirkland is desirable location relative to the other peer cities and that business owners are prepared to pay a premium for a Kirkland location presumably because they are able to generate higher business income in this location.

Whle the overall average land values in Kirkland are higher than many peer communities, there are significant differences in land values among Kirkland's various commercial districts. Exhibit 11 presents the estimated average land values for Kirkland's commercial business districts. As shown, there are several districts that are close to the overall city average, with the Central Business District and the North Market Corridor valued significantly higher than average and Totem Lake significantly lower.

Exhibit 11

Average Land Value per Square Foot (Commercial Zoning) by Kirkland Business District, 2010

Business District	Average Land Cost/SF
Kirkland (Citywide Commercial)	**$30.99**
Central Business District	$89.52
Houghton	$34.44
Juanita	$38.48
North Market Corridor	$67.00
Rose Hill	$36.75
Totem Lake	$17.58

Note: Land values are for commercial zoning within the district. Does not include Light Industrial Technology zoned parcels.

Source: King County, 2010; BERK, 2010

Exhibit 12 presents the percent of land cost for each of the development types for Kirkland overall as compared with the peer and neighbor jurisdictions.

Exhibit 12

Estimated Land Costs as a Percent of Total Project Cost

Development Type	Kirkland	Bellevue	Bothell	Kent	Redmond	Renton
Large Office Building	6.3%	7.9%	2.5%	2.0%	5.9%	3.0%
Medium Office Building	9.2%	11.6%	3.8%	3.1%	8.2%	4.5%
Big Box Retail	52.6%	59.6%	30.0%	26.8%	50.0%	33.6%
Strip Retail	44.2%	50.1%	22.6%	20.0%	40.8%	25.9%
Mixed Use Development	3.2%	4.0%	1.2%	1.0%	3.0%	1.4%

Source: King County, 2010; BERK, 2010

For higher cost projects, such as a large or medium office building or a mixed use building, the land costs are smaller percent of the overall project cost. However, for lower value projects, such as a big box development or smaller scale retail development, land costs makeup a larger share of the project's overall cost. A developer of these types of developments may realize significant cost savings by locating in lower cost jurisdiction.

Commercial rents. Rent is another cost of business that varies by location that can impact a business' location decision. This assessment used per square foot lease rates to calculate a representative business' annual rent. Lease rates are average asking lease rates from CB Richard Ellis' 2010 MarketView reports for the Puget Sound region. Exhibit 13 lists the lease rates used for this analysis.

Exhibit 13

Commercial Lease Rates (2010 Q1)

Type	Office Class A	Office Class B	Restaurant Retail
Kirkland	$28.42	$24.12	$16.88
Bellevue CBD	$33.89	$33.77	$28.74
Bellevue (Bel-Red)	$27.46	$23.74	$23.26
Bothell	$22.59	$22.05	$20.15
Kent	$21.61	$20.88	$23.10
Redmond	$24.58	$24.47	$29.53
Renton	$22.30	$20.51	$20.28

Source: CB Richard Ellis, MarketView - Puget Sound, 2010; BERK, 2010

CB Richard Ellis only has a broad "Retail" category for lease rates, thus, lease rates for the big box and restaurant representative business profiles are the same. The average retail lease rate used for Kirkland includes the Totem Lake area, which is likely to be lower than locations in downtown Kirkland. All lease rates for Bellevue are specific to the Bel-Red Corridor Commercial lease rates for the large and medium office profiles are based on the Class A lease rates.

High cost locations for commercial rent vary by the type of business. Exhibit 14 shows the annual rent paid for each representative business with the share of business' annual gross revenue its rent represents. For the large and medium office examples, Kirkland, followed closely by Bellevue, have the highest annual rents. For retail businesses, Redmond, Bellevue, and Kent are close together with the highest rents. Kirkland has the lowest annual rent.

Exhibit 14

Annual Rent & Rent as a Percent of Annual Gross Revenue

Business Type	Kirkland	Bellevue	Bothell	Kent	Redmond	Renton
Large Office	$1,278,900	$1,235,700	$1,016,550	$972,450	$1,106,100	$1,003,500
% of Gross Rev.	7.6%	7.4%	6.1%	5.8%	6.6%	6.0%
Medium Office	$375,144	$362,472	$298,188	$285,252	$324,456	$294,360
% of Gross Rev.	5.6%	5.4%	4.4%	4.2%	4.8%	4.4%
Restaurant	$288,648	$397,746	$344,565	$395,010	$504,963	$346,788
% of Gross Rev.	8.1%	11.2%	9.7%	11.1%	14.2%	9.7%
Big Box	$1,688,000	$2,326,000	$2,015,000	$2,310,000	$2,953,000	$2,028,000
% of Gross Rev.	2.9%	4.0%	3.5%	4.0%	5.1%	3.5%

Source: CB Richard Ellis, 2010; BERK, 2010

Rent is more substantial of a cost for a representative business then taxes. Depending on the business, annual rent paid represents 3-14% of a business' annual gross revenue**.**

Rents do vary somewhat between the peer cities. The restaurant example varies the most. The difference between the highest rent (Redmond) and the lowest (Kirkland) is $217,316, which represents 6.08% of the representative restaurant's gross revenue. For the large office example, the difference between the highest rent (Kirkland) and the lowest (Kent) is $306,450, which is 1.8% of its gross revenue.

A more temporal indicator of local competitiveness is the vacancy rates in office and retail space. Exhibit 15 presents the current vacancy rate for the peer and neighbor jurisdictions and compares these with some earlier data points. Clearly, the vacancy rates are showing the effects of the current major recession, as all of the communities are experiencing higher rates of vacancy.

In Kirkland, the vacancies are particularly high, which could be interpreted as an indicator that the City is not as competitive as the lease rate and land value data might suggest. It is worth looking a little bit beyond the raw numbers and considers some of the underlying issues that have led to these high levels of vacancy.

- The vacancies reflect the peculiarities of how the current recession has affected businesses throughout the region. Generally, these high vacancy rates reflect a significant drop in demand as businesses have contracted and some have closed. There is a certain element of luck involved in terms of how these reductions are spread among the various commercial areas.
- Before the recession, Kirkland enjoyed lower vacancies relative to the peer and neighbor jurisdictions
- The office vacancy is particularly high and likely reflects the impact of Google opening its own campus in late 2008 and pulled out of space elsewhere in the city. This shift, right as the overall economy was dropping into a major recession, would have had the effect of increasing the vacancy rate while keeping a major employer in the City.
- The retail vacancy rate is probably more troubling, since retail lease rates are already among the lowest within the peer and neighbor jurisdictions.

Exhibit 15

Office and Retail Vacancy Rates

	Office			Retail		
City	2003, Q4	2005, Q4	2010, Q1	2003, Q4	2005, H2	2009, Q4
Kirkland	9.3%	4.4%	30.6%	8.6%	0.8%	22.2%
Bellevue CBD	20.8%	9.1%	17.0%	1.5%	11.1%	4.4%
Bellevue (Non-CBD)*	10.1%	9.8%	11.1%	12.8%	2.9%	10.4%
Bothell	-	-	21.4%	0.9%	1.4%	4.6%
Kent	22.9%	24.5%	29.1%	1.9%	2.0%	7.5%
Redmond	11.6%	11.0%	25.7%	4.6%	0.3%	3.7%
Renton	23.6%	30.9%	14.0%	1.2%	0.9%	6.6%

*Bellevue office figures are for the Bel-Red corridor

Source: CB Richard Ellis, 2010; BERK, 2010

Council Meeting: 01/18/2011
Agenda: New Business
Item #: 11. b.

ORDINANCE 4288

AN ORDINANCE OF THE CITY OF KIRKLAND RELATING TO IMPACT FEES FOR CHANGES IN USE AND SUSPENDING TRANSPORTATION IMPACT FEES FOR CHANGES OF USE THAT DO NOT RESULT IN INCREASED FLOOR AREA.

The City Council of the City of Kirkland do ordain as follows:

Section 1. A new Kirkland Municipal Code Section 27.04.035 is hereby created to read as follows:

27.04.035 Temporary suspension of transportation impact fees relating to change of use

Notwithstanding any other provision of this Chapter, the City temporarily suspends the imposition of transportation impact fees to the extent the assessment of the fee is the result of a change to a land use category that results in a higher fee under KMC 27.04.150; provided that this Section shall not apply to a project to the extent it will add, increase or expand the gross floor area of an existing building; and provided further that this Section applies only to the use, renovation or remodeling of existing structures and does not apply to redevelopment projects or other projects in which existing structures are replaced or substantially redeveloped. This Section shall apply to projects for which complete building applications are filed with the City between February 1, 2011 and December 31, 2013. This Section shall automatically expire on December 31, 2013.

Section 2. If any provision of this ordinance or its application to any person or circumstance is held invalid, the remainder of the ordinance, or the application of the provision to other persons or circumstances is not affected.

Section 3. This ordinance shall be in force and effect five days from and after its passage by the Kirkland City Council and publication, as required by law.

Passed by majority vote of the Kirkland City Council in open meeting this 18th day of January, 2011.

Signed in authentication thereof this 18th day of January, 2011.

_____
MAYOR

Attest:

_____
City Clerk

Approved as to Form:

_____
City Attorney