



CITY OF KIRKLAND
Department of Finance & Administration
123 Fifth Avenue, Kirkland, WA 98033 425.587.3100
www.kirklandwa.gov

MEMORANDUM

To: Kurt Triplett, City Manager

From: Michael Olson, Director of Finance and Administration
Tom Mikesell, Financial Planning Manager

Date: September 9, 2016

Subject: PUBLIC HEARING ON REVENUE SOURCES FOR THE 2017-2018 BUDGET

RECOMMENDATION:

City Council hold a public hearing on revenue sources for the 2017-2018 Budget.

BACKGROUND:

This is the first of three scheduled public hearings on the 2017-2018 budget (two of which are required by statute). This first public hearing addresses revenue sources. The second and third public hearings on the 2017-2018 Preliminary Budget are scheduled to be held on Tuesday, November 1st and Tuesday, November 15th.

General Fund Projections

The City Council's last full briefing on the City's financial outlook was at its May 24, 2016 retreat. At that time, the forecast projected a \$79 thousand gap between ongoing revenues and expenditures in 2017-18, assuming the discontinuation of one-time service packages approved in the 2015-16 biennial and mid-biennial budget processes. An alternate forecast scenario was also discussed in which three items on the one-time list would be funded with ongoing resources as part of the June 21 mid-year budget adjustments, bringing the revised deficit projection to \$0.5 million. This list included:

- Enhanced Human Services Grant: \$45,262 per year;
- Public Disclosure Analyst: \$107,114 per year;
- Station 25 4th Firefighter (5 FTEs total): approximately \$636,800 in 2017 and \$556,806 in 2018, funded on an ongoing basis with annual revenues from the Emergency Transport Fee, which also funds ongoing administrative components of the transport program that total approximately \$263,000 per year. To help offset this change in use of general fund revenues, the annual transfer of \$375,000 to the Fire Public Safety Sinking Fund, will shift from ongoing to one-time funding. **(Note that if the final budget reconciliation results in sufficient additional on-going revenues, the City**

Manager will prioritize restoring the Fire Public Safety Sinking Fund contribution as on-going in the Preliminary 2017-2018 budget.)

At its June 21st Regular Meeting, Council approved the last two items as ongoing adjustments to the operating 2016 budget and they are now rolled into the base for 2017-2018. The Council also gave conceptual approval to the enhanced level of grant funding which was fully funded as one time money in 2015 and 2016. The Enhanced Human Services Grant will be included as an ongoing funding item in the Preliminary 2017-2018 Operating Budget. Together with these approved changes to the base budget, projections for 2017 and 2018 have been updated to reflect current information, including:

- An estimation of ongoing Salary and Wage budget reflecting settled collective bargaining agreements;
- An assessment of revenue collections under current economic conditions, based on departmental input;
- New information on contractually and/or statutorily derived rates; and,
- Basic budget information supporting current service levels as submitted by departments in August.

This updated financial projection provides the basis for budget meetings with the City Manager's Office, which are currently in progress. The 2017-2018 budget is being developed under the following principles:

- Stay steady given the long-term revenue outlook:
 - The rules for using REET flexibility have changed since the last budget cycle. As provided in RCW 82.46.010(7) and 82.46.035(7), selective REET use for maintenance of existing REET eligible capital facilities, defined by state law as follows:
 - "Labor and materials that will preserve, prevent the decline of, or extend the useful life of a capital project. Maintenance *does not* include labor or material costs for routine operations of a capital project (emphasis added)."
 - Prepare for the end of the State annexation sales tax credit in 2021;
 - Continue to budget sales tax on a modified two-year lag and set aside a portion of sales tax revenue growth toward one time uses.
- Service packages (program additions) will be viewed in the context of reprioritizing or trade-offs. Said another way, proposed additions will be evaluated in the context of whether they can be supported by new revenues or through reductions in lower priority programs. The list of currently one-time funded positions and programs will be evaluated in this context as well.
- Setting aside funds towards:
 - Unfunded capital needs rather than spending available General Funds solely on operations.
 - Temporary resources to address workload backlogs

- Keep non-personnel expenditure cost growth to zero, with the exception of known external contractual obligations or other expected cost increases (e.g., fuel, utilities) that cannot be offset by savings elsewhere.
- Resource needs to meet the demands of increased development activity continue to be evaluated and short and long-term adjustments will be reviewed and proposed as part of the budget process.

Staff is currently developing the revenue and expenditure projections for the Preliminary 2017-2018 Budget. Main factors that we are reviewing in this process include:

- The 2017 and 2018 Salaries and Wages budget realizes two years of attrition savings that was not reflected in the May forecast. The May forecast was based on 2016 budget levels, which were established using the staffing roster in effect in the fall of 2014. As long tenured employees retire, often paid at the top salary step and longevity rate, they are replaced by new employees at the bottom step, resulting in natural turnover savings. Kirkland has seen a significant number of retirements in 2015 and 2016 and will be realizing substantial savings on a position by position basis;
- Higher than forecast revenues from Punch Board and Card Games, based on strong 2015 and 2016 collections activity raising the baseline for 2017 and 2018;
- Higher than forecast revenues from development licensing and permitting are projected for 2017 and 2018 which will either be used for resources to meet workload or set aside in reserve;
- Higher than forecasted revenues from CIP Engineering charges, largely due to the impact of additional billed hours by the 5 CIP Project Engineering staff added in fall 2015; and,
- Lower than forecasted expenditures for NORCOM services.

Below is a more detailed discussion of current revenue and expenditure assumptions and a calendar of next steps in the budget process.

Revenue Assumptions

The current 2017-2018 projection is based on a number of revenue assumptions, including:

- **Reserves** - No use of general purpose reserves in 2017-2018;
- **Property Tax** – 1.0% optional increase each year and 1.0% annual growth in new construction property tax. The new construction estimate for 2017 will be updated when information becomes available from the King County Assessor;
- **Sales Tax**
 - General Fund 2016 sales tax revenue is projected at over 5.0 percent ahead of 2015 actual results. Year-to-date total sales tax collections through July are 6.9

percent ahead of 2015 as detailed in the August Sales Tax Revenue report (Attachment A); and,

- No increase in sales tax is projected for 2017 and 2018, reflecting the policy-based modified two-year lag.
- **Annexation Sales Tax Credit** – Support from tax credit is projected to remain at 2016 levels in 2017 and 2018;
- **Utility Tax**
 - No growth in Private utility tax collections is projected in 2017 and 2018, reflecting uncertainty in future utility rate trends and weather-related consumption patterns;
- **Revenue Generating Regulatory License** –This fee has remained unchanged since implementation in 2009. Revenues are expected to grow 1% in 2017 and 2018; The City Manager is proposing to increase the RGRL fee by \$5 dollars (from \$100 to \$105) per employee or FTE to provide revenue to help support the public safety investments that are proposed for Police and Fire.
- **Development-related revenues** are estimated to remain at or above near their 2016 levels into 2017 and drop moderately in 2018, reflecting continuing strength in development in the near term but acknowledging the likely maturation of the development cycle in the second year of the biennium; and,
- **Interest earnings** have been adjusted to reflect the impact of investment advisor services, including active portfolio management on interest earnings rates.

These assumptions are based on the revenue trends through June 30, 2016 as noted in the second quarter 2016 Financial Management Report (see Attachment B), collections experience through July, and current economic projections. Further refinements in revenue estimates may occur throughout the budget deliberation process as new data becomes available.

Expenditure Assumptions

The updated projections also reflect the following expenditure assumptions, including:

- **Full Staffing** - All the ongoing positions budgeted in 2016 are budgeted in 2017-2018;
- **Excludes One-time Service Packages** - There are one-time expenditures budgeted in 2015-2016 that likely will be considered for continuation in the 2017-18 budget process. As mentioned in the May forecast memo, the continuation of all of the current services would cost about \$1.3 million per year. These costs are not included in this forecast, and are detailed in the following table:

One Time Items Likely to Continue	2015			2016		
	Wages & Benefits	Other Costs	Annual Costs	Wages & Benefits	Other Costs	Annual Costs
Public Safety Sinking Fund Transfer		375,000	375,000		375,000	375,000
Subtotal	-	375,000	375,000	-	375,000	375,000
Previously Funded with Resources Forward (or) Surplus						
2016 Community Survey	-	-	-	-	30,000	30,000
ARCH Housing Trust Fund	-	315,000	315,000	-	315,000	315,000
City Match Events Funding	-	32,000	32,000	-	32,000	32,000
Cultural Organizations Grant Matching one-time	-	5,000	5,000	-	5,000	5,000
Human Services Option #3	-	58,113	58,113	-	58,113	58,113
Inmate Medical	-	108,332	108,332	-	113,862	113,862
KAN additional grants	-	5,101	5,101	-	5,101	5,101
Kirkland Heritage Society preservation efforts	-	2,000	2,000	-	2,000	2,000
Leadership Eastside Scholarships	-	12,000	12,000	-	12,000	12,000
Municipal Court Security	67,176	-	67,176	67,176	-	67,176
Neighborhood Traffic Control Coordinator	57,002	281	57,283	59,790	281	60,071
Office Tech - Training Division	34,325	(12,401)	21,924	35,776	(13,127)	22,649
Public Records Request Assistance	13,173	-	13,173	13,296	-	13,296
KPC Operating Support	-	50,000	50,000	-	50,000	50,000
Social Worker at John Muir Elementary one-time	-	11,752	11,752	-	11,752	11,752
State Legislative Advocacy Services Mid Biennial	-	3,000	3,000	-	12,000	12,000
State Legislative Advocacy Services Service Package	-	48,000	48,000	-	48,000	48,000
Time Bank	-	3,000	3,000	-	3,000	3,000
Subtotal	171,676	648,178	819,854	176,038	684,982	861,020
Total	171,676	1,023,178	1,194,854	176,038	1,059,982	1,236,020

- **COLA Reserve** – Collective bargaining agreements with AFSCME and Teamsters are in effect through 2017, and will be open in 2018. Agreements with all other bargaining groups are open in both 2017 and 2018. A reserve has been set-aside for potential annual raises of 2% per year in anticipation of settling those contracts;
- **Debt** - Approximately \$0.4 million per year is budgeted to pay for City hall debt issued in 2015 and \$2.1 million is budgeted to repay debt for the Kirkland Justice Center;
- **Benefit Inflation – For 2017** the budget assumes no increase in health benefits costs for the prime and high deductible plans, and increases based on the rates given by the providers are included for the Group Health, vision and dental plans. For 2018, a 2% increase is assumed for all health benefits. Increases to retirement contribution rates are included as determined by the Department of Retirement Services;
- **Reserve Replenishment** - Continuing planned reserve replenishment of one-percent of General Fund revenue results in a total of \$1.8 million of the projected 2017-2018 operating revenues being set aside toward the reserve target level based on the Council’s reserve replenishment principles as adopted by resolution (R-4900);
- **Current Services Levels** - No new one-time or ongoing service packages are reflected. The City Manager is currently reviewing services package requests submitted by departments and his recommendations will be reflected in the preliminary budget; and,
- **General Fund Capital Contribution** – Assumes transfer of \$1.7 million of 2015 year end cash to the Capital Improvements Fund to pay a portion of Fire Station 24 construction costs, and amounts for ongoing contributions for GIS capital projects and emergency generators every other year in the biennium.

As with the revenue assumptions, these will be subject to refinement during the budget process. In addition, an updated forecast will be included as part of the budget process.

Budget Process

A balanced preliminary budget, reflecting the City Manager's recommendations, will be available to the City Council and the public on October 21. The following list includes this and other significant dates in the 2017-18 budget process.

- October 21 – 2017-2018 Preliminary Budget provided to the City Council/public
- October 25 - Finance & Administration Committee budget update
- October 27 – Council Budget Work Session (3-9 pm)
- November 1 – Additional budget study session and public hearing
- November 7 – Additional budget study session (if needed)
- November 15 – Public hearing on the Preliminary 2017-2018 Budget and preliminary 2017 property tax levy
- December 13 – Adoption of 2017-2022 CIP, 2017-2018 Budget, and final 2017 property tax levy



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MEMORANDUM

To: Kurt Triplett, City Manager

From: Michael Olson, Director of Finance & Administration
 Tom Mikesell, Financial Planning Manager
 Elijah Panci, Budget Analyst

Date: September 13, 2016

Subject: August Sales Tax Revenue

August results reflect sales activity in June, due to the two month lag in reporting sales tax data. Sales tax revenue is **up 3.1 percent** compared to August 2015. Month-over-month growth continued for an eighth consecutive month this year. Despite continued growth, the outlook is not encouraging as several sectors declined, most notably Auto/Gas Retail. Contracting continues to be the one sector compensating for underperformance in other sectors.

The year-to-date growth, which had been steadily declining over the past few months, fell more significantly in August, and is now down to **6.9 percent**.

The following sections discuss the highlights by business sector details of both the month-to-month and year-to-date results. Also included are observations of sales tax collections in our neighboring cities, as well as a discussion of key economic variables that impact sales taxes.

Comparing August 2016 to August 2015

Comparing collections from the month of August this year and last provides insight into business sector performance controlling for seasonal cycles in sales.

2016 Sales Tax Receipts by Business Sector-Monthly Actuals

Business Sector Group	August		Dollar Change	Percent Change	Percent of Total	
	2015	2016			2015	2016
Services	235,609	233,390	(2,219)	-0.9%	13.7%	13.2%
Contracting	292,273	350,370	58,097	19.9%	17.0%	19.8%
Communications	40,187	49,329	9,142	22.7%	2.3%	2.8%
Retail:						
Auto/Gas Retail	401,122	374,018	(27,104)	-6.8%	23.4%	21.1%
Gen Merch/Misc Retail	171,547	165,465	(6,082)	-3.5%	10.0%	9.4%
Retail Eating/Drinking	148,341	144,822	(3,519)	-2.4%	8.6%	8.2%
Other Retail	234,433	253,890	19,457	8.3%	13.7%	14.4%
Wholesale	95,168	83,984	(11,184)	-11.8%	5.5%	4.7%
Miscellaneous	96,663	113,939	17,276	17.9%	5.6%	6.4%
Total	1,715,342	1,769,207	53,864	3.1%	100%	100%

Comparing month-to-month, August sales tax collections this year are **\$53,864 (3.1 percent)** higher than August 2015.

In terms of dollar growth, **Contracting** performed best compared to August 2015, increasing by **\$58,000 (19.9 percent)**. The top three improving sectors were rounded out by **Other Retail**, which was up **\$19,000 (8.3 percent)** and **Miscellaneous**, which grew **\$17,000 (17.9 percent)**.

Though month-over-month growth is positive, most groups declined, and a strong month from Contracting is yet again the main reason for month-to-month growth. Growth in Miscellaneous was driven by Real Estate, which had another strong month, up \$12,000 (41.7 percent) from August 2015. Furniture sales, up \$12,000 (43.2 percent), was the main reason for growth in Other Retail. Food & Beverage sales also contributed to growth, increasing \$6,000 (17.5 percent) month-to-month.

Several groups fell this month, led by **Auto/Gas Retail, which fell \$27,000 (6.8 percent)**. Rounding out the top three were **Wholesale, which was down \$11,000 (11.8 percent)**, and **General Merchandise/Misc Retail, which was down \$6,000 (3.5 percent)**.

Auto/Gas Retail has now declined three out of the past four months. This is a concern because this group is the largest source of sales tax revenue for the City and is a leading indicator of economic conditions. Though the decreases in other groups were not excessively large nor individually indicative of negative trends, the fact that five out of the nine groups decreased is not encouraging.

Though the growth rate remains positive this month, the outlook is concerning. Contracting growth, which usually does not follow other economic trends, has inflated otherwise pedestrian growth rates for much of the year.

Year-to-Date Review

Year-to-date sales tax totals are useful for comparing revenues received so far this year with last year's totals through the same period. This information gives context on each sector's longer term performance and allows developing trends to be identified.

City of Kirkland Actual Sales Tax Receipts

Business Sector Group	YTD		Dollar Change	Percent Change	Percent of Total	
	2015	2016			2015	2016
Services	1,631,786	1,758,927	127,141	7.8%	13.3%	13.4%
Contracting	1,877,605	2,174,751	297,146	15.8%	15.3%	16.6%
Communications	275,333	355,926	80,593	29.3%	2.2%	2.7%
Retail:						
Auto/Gas Retail	3,093,215	3,112,618	19,403	0.6%	25.2%	23.7%
Gen Merch/Misc Retail	1,404,772	1,354,715	(50,057)	-3.6%	11.4%	10.3%
Retail Eating/Drinking	1,015,391	1,047,615	32,224	3.2%	8.3%	8.0%
Other Retail	1,650,536	1,839,713	189,177	11.5%	13.4%	14.0%
Wholesale	625,230	661,602	36,372	5.8%	5.1%	5.0%
Miscellaneous	701,731	818,968	117,237	16.7%	5.7%	6.2%
Total	12,275,600	13,124,833	849,233	6.9%	100%	100%

Through the end of August, year-to-date sales tax revenues are up **6.9 percent**. This is 0.7 percentage points lower than the year-to-date growth rate reported in July.

By dollar amount, the largest growth is in **Contracting**, which is up **\$297,000 (15.8 percent)** from last year. **Other Retail** and **Services** are the next two leading sectors, up **\$189,000 (11.5 percent)** and **\$127,000 (7.8 percent)** respectively. Contracting has consistently performed well on the year despite being a volatile group, and accounts for 35 percent of year-to-date growth. Other Retail has

consistently been one of the top growth groups in 2016, while Services remains in the top three despite seeing a slight month-over-month decline in August.

Despite a slow month for many groups, **General Merchandise/Misc Retail** is the only group down on the year, **50,000 (3.6 percent)** below 2015 revenues. Receipts are down marginally for most major retailers in the Misc Retail category, which accounts for \$41,000 of the decrease. Though it is the only sector to decline, it is one of the largest sectors and an important contributor to the City's sales tax revenue.

Also worth noting is the falling year-to-date growth of **Auto/Gas Retail**, which is now down to 0.6 percent. The growth rate was up to 6.4 percent in April, before a four month slide in which the year-to-date growth rate fell 5.6 percentage points.

Neighboring City Performance

Though neighboring cities are performing well this year, August was a down month for most of the surrounding cities. Year-to-date growth decreased for Bothell, Bellevue, Renton, and Seattle by 0.9, 1.5, 0.1, and 0.5 percentage points respectively. Each city's month-over-month growth rate was positive, but most of them were at least 5 percentage points lower than the previous month, except for Renton which was down just 0.8 percent. Sales tax revenue was low throughout the entire region in August. Even Redmond had a relatively down month in comparison to the rest of the year, as month-over-month growth was 33.0 percent, the third smallest growth rate of 2016 for the city. However, the year-to-date growth rate remained high at 46.6 percent.

National and Regional Economic Context:

Information about wider trends in the economy provides a mechanism to help understand current results in Kirkland, as well as predict future performance. The combination of consumer confidence, unemployment levels, housing data and auto sales provide the broader economic context for key factors in sales tax revenues. The following table includes the most recently available data and prior month's readings, for some of the most relevant indicators.

2016 Wider Economic Indicators					
Indicator	Most Recent Month of Data	Unit	Month		
			Current	Previous	Change
<i>Consumer Confidence</i>					
Consumer Confidence Index	August	Index	101.1	97.3	3.8
<i>Unemployment Rate</i>					
National	August	%	4.9	4.9	0.0
King County	July	%	4.4	4.3	0.1
<i>Housing</i>					
New House Permits	July	Thousands	39.8	47.7	(7.9)
Seattle Area Home Prices	June	Index	202.6	199.9	2.7
<i>Inflation (CPI-W)</i>					
National	July	% Change	1.0	0.6	0.4
Seattle	June	% Change	2.0	2.6	(0.6)
<i>Car Sales</i>					
New Vehicle Registrations	August	Thousands	25.2	25.3	(0.1)

The Conference Board reported an increase for the **Consumer Confidence Index** in August, as the Index jumped 3.8 points to 101.1. The Board reports that consumers feel more positive about current conditions and the near-term outlook.

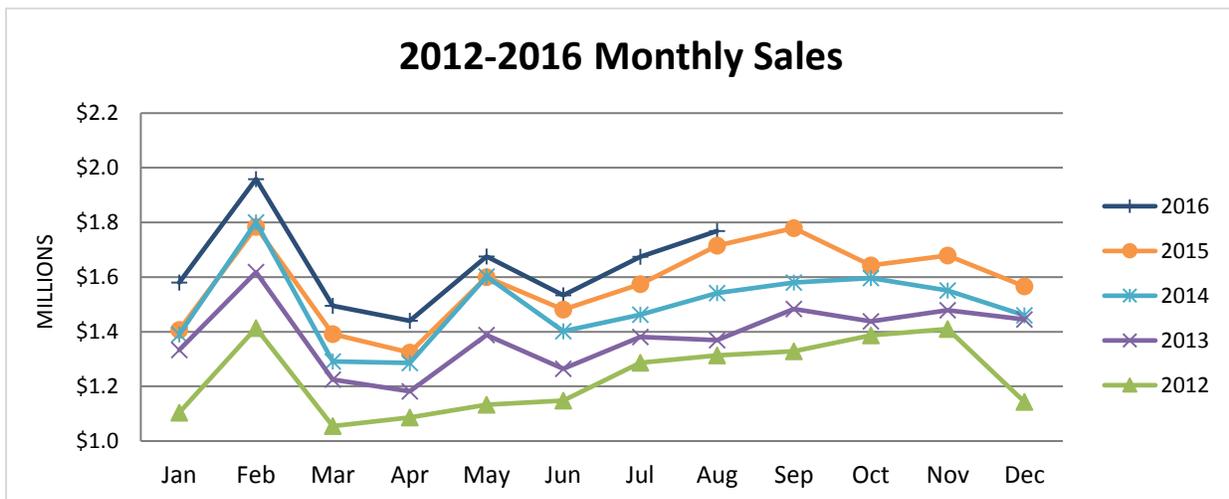
Unemployment Rates were static at the National level, remaining at 4.9 percent from July to August. The unemployment rates in Washington State, King County, and Kirkland each increased 0.1 percentage points, but remain close to the yearly low points for each respective jurisdiction.

The latest data on statewide **New House Permits** shows a significant decrease, down to 39,800 permits in July from 47,700 permits in June. The number of new permits has been volatile from month to month in 2016, but the average remains similar to 2015, which was a strong year for housing permits. The latest data for the **Seattle Area Home Price Index** shows another increase, up to 202.6 in June from 199.9 in May. Seattle area housing prices continue to grow at a rapid pace, increasing 8.4 percent since January.

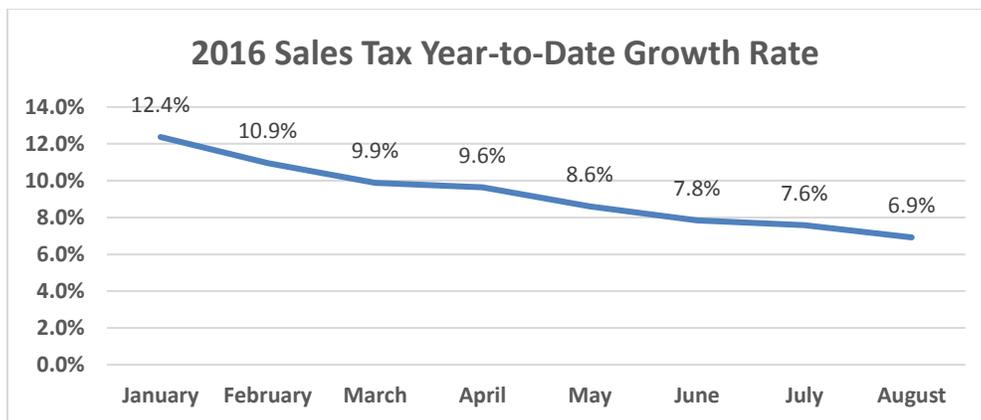
New Vehicle Registrations decreased slightly again in August, down by 100 to 25,200. While registration levels remain relatively high, they have slowly decreased since the two year high water mark of 28,400 in January.

Conclusion

The following chart shows Kirkland’s monthly sales tax revenues through June.



Sales tax revenue in 2016 continues to outperform revenue in 2015, but by a diminishing margin. The year-to-date growth rate has declined every month since January. Current indicators and trends do not suggest that pattern will change. The strong start to 2016 has worn off, and low or negative month-over-month growth rates may be in store for the last few months of 2016.





Financial Management Report as of June 30, 2016

AT A GLANCE:

Solarize Kirkland program encourages community buying power (page 2)

2016 second quarter general fund revenues increased 8.2% over 2015 (page 3)

Sales tax revenue grew 7.8% in the second quarter (page 5)

Unemployment is static, Seattle inflation grows, and the housing market continues to improve (pages 7-8)

The City's portfolio outperformed both the 90 day T Bill and the 2 year rolling average of the 2 year Treasury note (page 8)

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Summary of All Operating Funds: *Revenue*

- General Fund** revenue ended June **8.2 percent ahead** of 2015, an increase of \$3,610,349. The increase is largely the result of higher Planning Check Fees, Sales Taxes and Revenue Generating Regulatory Licenses. Actual revenues finished the quarter at 53.7 percent of budget, 50 percent of the way through the year. A more detailed analysis of General Fund revenue can be found on page 3, and details on sales tax revenue begin on page 5.
- Other General Government Funds** revenue finished the quarter **5.2 percent higher** than 2015, up \$695,164. **The Information Technology Fund and Street Operating Fund** accounted for the majority of the growth, up **7.2 and 5.4 percent** respectively. Information Technology Fund revenue grew largely due to charges received for temporary GIS services provided in support of the Lucity Enterprise Asset Management project, while the Street operating Fund revenue grew largely due to two factors, including higher gas tax revenue as a result of state legislative increases in fall 2015 and an insurance recovery for a traffic signal that was knocked down on Willows Road.
- Actual revenue for total Other Government revenues, excluding interfund transfers, was at 52.2 percent of budget. All funds, with the exception of Lodging Tax, were at or above 50%; Lodging tax was 40% of budget due to seasonality of Hotel and Motel Tax receipts, the majority of which are collected in the late summer and early fall.
- Water/Sewer Operating Fund** second quarter revenue is **up 1.4 percent** from 2015. Actual revenue for the quarter was **45.3 percent of budget**. Growth over 2015 is largely due to higher collections from commercial and residential sewer usage charges.
- Surface Water Management Fund** revenues finished June at **53.9 percent of budget**. Revenues through the second quarter of 2016 were **2.1 percent lower** than they were during the same period in 2015. The decrease is due to lower grant revenue in 2016. In 2015, the City received grant revenue from the Department of Ecology for local source control and the Environmental Protection Agency for Totem Lake/Juanita Creek Basin storm water control design. Excluding the impacts of these grants, revenue would otherwise be 1.8 percent higher than in 2015, led by growth in Storm drainage fees.
- Solid Waste Fund** finished the first half of the year with **49.5 percent of budgeted revenues**. Actual revenues were 1.8 percent higher than in 2015. Commercial collection led the way, with 4.2 percent higher collections in 2016.
- Overall, utility fund revenues through the second quarter were **up 0.8 percent** compared to 2015, and finished the first half of 2016 at **48.2 percent of budget**.

Resources by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2015	6/30/2016	% Change	2015	2016	% Change	2015	2016
General Gov't Operating:								
General Fund	43,965,832	47,576,181	8.2%	86,443,318	88,658,144	2.6%	50.9%	53.7%
Other General Gov't Operating Funds	13,421,895	14,117,059	5.2%	26,531,966	27,050,873	2.0%	50.6%	52.2%
Total General Gov't Operating	57,387,727	61,693,240	7.5%	112,975,284	115,709,017	2.4%	50.8%	53.3%
Utilities:								
Water/Sewer Operating Fund	12,018,020	12,185,914	1.4%	26,451,995	26,905,563	1.7%	45.4%	45.3%
Surface Water Management Fund	5,530,845	5,414,122	-2.1%	9,939,650	10,047,501	1.1%	55.6%	53.9%
Solid Waste Fund	8,149,159	8,318,464	2.1%	16,445,443	16,853,760	2.5%	49.6%	49.4%
Total Utilities	25,698,024	25,918,500	0.9%	52,837,088	53,806,824	1.8%	48.6%	48.2%
Total All Operating Funds	83,085,751	87,611,740	5.4%	165,812,372	169,515,841	2.2%	50.1%	51.7%

*Budgeted and actual revenues exclude resources forward and interfund transfers.

Kirkland Paves the Way for Online Commerce

Thanks to a grant awarded by the Washington State Department of Commerce, the City of Kirkland, in partnership with Pacific Northwest Pollution Prevention Resource Center (PPRC), will be conducting outreach to neighborhoods and businesses about a solar purchasing program. Solarize Kirkland is designed to encourage a group purchase, or "bulk buy," of solar arrays and the campaign aims to help Kirkland residents and businesses achieve an affordable and successful solar installation. The program provides a reduced cost and easy installation of solar panels on homes, businesses, and multi-family units. The City will host two informational workshops for home and business owners and property managers: July 16 and August 11, from 7 to 9 p.m., at Kirkland City Hall, Council Chambers, 123 Fifth Avenue. Two other workshops will be held in September, but are not yet scheduled.

This type of program has been widely successful in many locations including Seattle, Snohomish County, and more broadly on a national scale, from Portland to New York – with savings as much as 20% on average when compared to acquiring solar systems independently.

Summary of All Operating Funds: *Expenditures*

- **General Fund** expenditures (excluding transfers) finished the second quarter of 2016 **up 3.5 percent** from the year before. Actual expenditures finished at **48.9 percent of budget**. Intergovernmental Professional Services led the growth with a \$656,278, or 40 percent, increase over last year. This is because of a one-time pass through payment made to Bellevue related to the 'A Regional Coalition for Housing' project. Personnel services grew 2.8 percent above last year, due to movement through salary steps and collective bargaining contract increases. An analysis of General Fund expenditures by department can be found on pages 4 and 5.

Other General Government Operating Funds actual expenditures were **9.5 percent higher** than 2015, largely due to increases in the Street Operating Fund. Street Operating Fund expenditures **increased 35.7 percent** due to the hiring of temp employees, increased Utility Services charges for a full year of street light funding in the annexed area, and Capital Outlays. Capital Outlays expenditures in 2016 were for median landscaping improvements, originally budgeted in 2015. The Parks Levy Fund spent less than in 2015, **falling 10.7 percent**, due to the Green Kirkland program. In aggregate, other general government operating funds finished the first half of 2016 at **44.2 percent** of budgeted funds.

- **Water/Sewer Operating Fund** actual expenditures through the first half of the year were **4.1 percent higher** than in 2015. This was largely because of an increase in the Metro Sewer Charge, as well as expenditures on Other Services. Increases in Other Services were mostly for Professional Services related to the update of the Sewer Master Plan, which was originally budgeted for 2015. In total, the Water/Sewer fund finished June at **48.6 percent of budget**.
- **Surface Water Management Fund** expenditures at the end of the first quarter were **4.3 percent higher** than 2015. This increase is from salaries and benefits. Expenditures for labor were up through the second quarter due to acceleration of the work load for the Cochran Springs project. Surface Water Management's non personnel services spending was lower by comparison, due largely to higher one-time professional services spending in 2015 on grant funded work, including the Totem Lake/Juanita Creek basin design project and the Local Source Control program. Expenditures through the end of June were **lower than budgeted, at 45.6 percent** of budget.
- **Solid Waste Fund** expenditures through June were **1.4 percent higher** in 2016 than in 2015. Small increases in expenditures for the waste disposal contract (which was planned), personnel, and external taxes were the cause of the overall increase. Expenditures in the fund finished the second quarter at **49.9 percent of budget** which is in line with expected budget expenditures.

Expenditures by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2015	6/30/2016	% Change	2015	2016	% Change	2015	2016
General Gov't Operating:								
General Fund	39,323,443	40,706,873	3.5%	83,534,621	83,209,548	-0.4%	47.1%	48.9%
Other General Gov't Operating Funds	9,509,722	10,412,748	9.5%	25,071,855	23,561,956	-6.0%	37.9%	44.2%
Total General Gov't Operating	48,833,164	51,119,621	4.7%	108,606,476	106,771,504	-1.7%	45.0%	47.9%
Utilities:								
Water/Sewer Operating Fund	10,698,547	11,132,137	4.1%	22,929,938	22,912,557	-0.1%	46.7%	48.6%
Surface Water Management Fund	3,194,984	3,333,006	4.3%	7,877,204	7,305,840	-7.3%	40.6%	45.6%
Solid Waste Fund	7,975,613	8,084,646	1.4%	16,065,707	16,210,048	0.9%	49.6%	49.9%
Total Utilities	21,869,144	22,549,789	3.1%	46,872,849	46,428,445	-0.9%	46.7%	48.6%
Total All Operating Funds	70,702,308	73,669,409	4.2%	155,479,325	153,199,949	-1.5%	45.5%	48.1%

*Budgeted and actual expenditures exclude working capital, operating reserves, capital reserves, and interfund transfers.

General Fund Revenue

- **Sales tax** revenue allocated to the General Fund through the second quarter of 2016 was **7.8 percent higher** than it was in 2015. The bulk of this increase is in the Contracting, Other Retail, and Miscellaneous sectors. A detailed analysis of total sales tax revenue can be found starting on page 5.
- **Property taxes** through June were **2.9 percent higher** than 2015, **at 53.2 percent of budget**. This increase is slightly higher than budgeted growth expectations for the year, though this difference is likely due to the timing of payments.
- **Utility tax** collections finished June **flat** compared to results through June 2015. Growth in electric utility taxes were offset by declines in gas and telecommunications. Collections through June were at **49.6 percent** of budget.
- **Other taxes** actual revenues were **6.6 percent higher** than in 2015, and finished at **69.3 percent of budget**. This increase is the result of higher revenues from Punch Board, Pull Tabs, and Card Games.
- The **business licenses (base fee) and franchise fees** were **4.4 percent** higher than in 2015 and finished June **at 52.5 percent** of budget.
- Collections from the **revenue generating regulatory license fee** were **35.8 percent higher** than in 2015. Revenues were at **70.8 percent of budget**. A portion of this growth is one-time revenue, as the City identified businesses operating without licenses, some of them owing up to three years of back payments.
- **Plan check fees and planning fees** finished the quarter **up 86 percent** and **81.5 percent** respectively. **Building, Structural and Equipment permits** were **up 5.7 percent** and **Engineering Services charges** were **down 5.6 percent** compared to 2015. Much of the Planning Fee increases are due to activity at Totem Lake and Kirkland Urban, while the Building permit increase stems from a rush in activity in advance of a building code change in July. The drop in Engineering Services is related to abnormally high revenues in 2015 from Google Campus Phase 2 Expansion.
- **Fines and Forfeitures** were **down 15.8 percent from 2015** due to a decrease in both Traffic and Parking Infraction Penalties. However, an increase in Business License Penalties offset much of the lost revenue elsewhere. This revenue source finished June **at 34.5 percent of budget**. Traffic infraction penalties are not receipted in January, so the budget is collected in 11 months from February to December. Therefore, this category will be closer to budget by year end if past trends hold for the current year.
- **Miscellaneous** revenue finished March **15.7 percent up** from 2015 due to higher interest earnings and increased revenue from rental properties, most notably from the Yuppie Pawn Shop property. This category was **above budget projections at 87.9 percent of budget**.

General Fund revenues ended the second quarter \$3,610,348 higher than in 2015 largely due to growth in taxes and charges for services.

The General Fund is the largest of the General Government Operating funds. It is primarily tax supported and accounts for basic services such as public safety, parks and recreation, and community development.

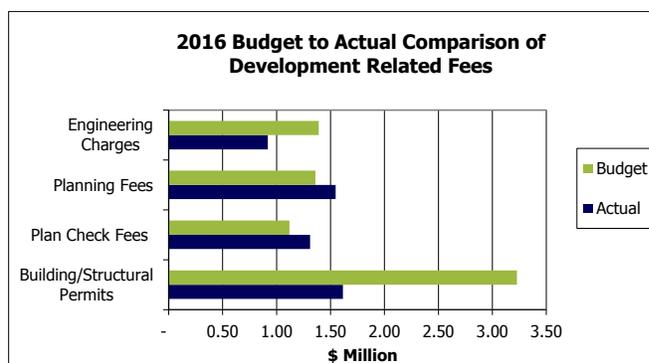
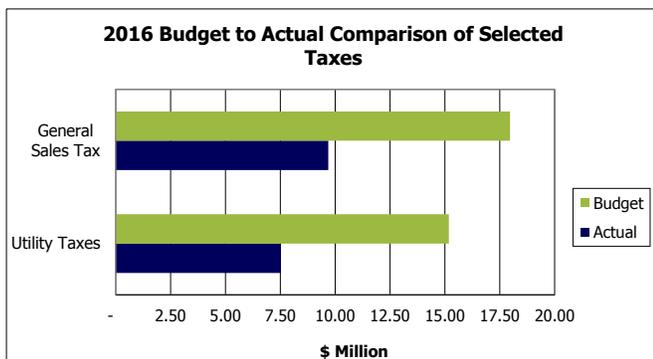
Many significant General Fund revenue sources are economically sensitive, such as sales tax and development-related fees.

About 441 of the City's 580 regular employees are budgeted within the general fund this year.

General Fund Resource Category	Year-to-Date Actual			Budget			% of Budget	
	6/30/2015	6/30/2016	% Change	2015	2016	% Change	2015	2016
Taxes:								
Retail Sales Tax: General	8,986,333	9,684,732	7.8%	17,963,747	17,963,747	0.0%	50.0%	53.9%
Retail Sales Tax Credit: Annexation	1,503,302	1,574,244	4.7%	3,792,500	3,935,000	3.8%	39.6%	40.0%
Retail Sales Tax: Criminal Justice	1,001,583	1,099,881	9.8%	2,036,370	2,097,461	3.0%	49.2%	52.4%
Property Tax	9,243,806	9,515,458	2.9%	17,456,855	17,886,952	2.5%	53.0%	53.2%
Utility Taxes	7,526,842	7,525,779	0.0%	15,015,081	15,175,950	1.1%	50.1%	49.6%
Rev Generating Regulatory License	1,233,338	1,674,558	35.8%	2,338,315	2,364,399	1.1%	52.7%	70.8%
Other Taxes	697,199	742,893	6.6%	1,063,075	1,072,758	0.9%	65.6%	69.3%
Total Taxes	30,192,403	31,817,546	5.4%	59,665,943	60,496,267	1.4%	50.6%	52.6%
Licenses & Permits:								
Building, Structural & Equipment Permits	1,528,627	1,615,401	5.7%	3,219,731	3,227,201	0.2%	47.5%	50.1%
Business Licenses/Franchise Fees	2,300,740	2,402,699	4.4%	4,532,649	4,580,520	1.1%	50.8%	52.5%
Other Licenses & Permits	301,407	306,677	1.7%	444,563	519,801	16.9%	67.8%	59.0%
Total Licenses & Permits	4,130,774	4,324,777	4.7%	8,196,943	8,327,522	1.6%	50.4%	51.9%
Intergovernmental:								
Grants and Federal Entitlements	103,993	90,229	-13.2%	162,125	132,000	-18.6%	64.1%	68.4%
State Shared Revenues & Entitlements	569,308	671,527	18.0%	1,098,514	1,339,360	21.9%	51.8%	50.1%
EMS	0	0	N/A	902,338	920,385	2.0%	N/A	N/A
Total Intergovernmental	673,301	761,756	13.1%	2,162,977	2,391,745	10.6%	31.1%	31.8%
Charges for Services:								
Internal Charges	2,924,575	3,397,643	16.2%	6,159,409	7,116,620	15.5%	47.5%	47.7%
Engineering Services	972,401	917,678	-5.6%	1,400,887	1,391,146	-0.7%	69.4%	66.0%
Plan Check Fee	704,823	1,311,062	86.0%	951,346	1,118,880	17.6%	74.1%	117.2%
Planning Fees	851,957	1,546,363	81.5%	1,457,383	1,359,493	-6.7%	58.5%	113.7%
Recreation	931,978	954,786	2.4%	1,215,100	1,215,200	0.0%	76.7%	78.6%
Other Charges for Services	958,846	948,049	-1.1%	1,980,204	2,093,739	5.7%	48.4%	45.3%
Total Charges for Services	7,344,579	9,075,580	23.6%	13,164,329	14,295,078	8.6%	55.8%	63.5%
Fines & Forfeits	898,008	755,977	-15.8%	2,189,359	2,191,067	0.1%	41.0%	34.5%
Miscellaneous	726,768	840,543	15.7%	1,063,767	956,465	-10.1%	68.3%	87.9%
Total Revenues	43,965,832	47,576,181	8.2%	86,443,318	88,658,144	2.6%	50.9%	53.7%
Other Financing Sources:								
Interfund Transfers	0	0	N/A	437,228	334,266	-23.5%	N/A	N/A
Total Other Financing Sources	0	0	N/A	437,228	334,266	-23.5%	N/A	N/A
Total Resources	43,965,832	47,576,181	8.2%	86,880,546	88,992,410	2.4%	50.6%	53.5%

*Budgeted and actual revenues exclude resources forward.

General Fund Revenue *continued*



General Fund Expenditures

General Fund Department Expenditures	Year-to-Date Actual			Budget			% of Budget	
	6/30/2015	6/30/2016	% Change	2015	2016	% Change	2015	2016
Non-Departmental	1,052,974	919,054	-12.7%	2,943,258	2,372,324	-19.4%	35.8%	38.7%
City Council	288,481	319,729	10.8%	473,818	497,615	5.0%	60.9%	64.3%
City Manager's Office	855,295	1,170,405	36.8%	2,438,154	2,172,715	-10.9%	35.1%	53.9%
Municipal Court	1,187,391	1,224,459	3.1%	2,445,952	2,456,641	0.4%	48.5%	49.8%
Human Resources	706,357	730,527	3.4%	1,492,619	1,541,006	3.2%	47.3%	47.4%
City Attorney's Office	673,491	623,066	-7.5%	1,246,620	1,173,872	-5.8%	54.0%	53.1%
Parks & Community Services	3,473,586	3,442,923	-0.9%	8,423,620	7,973,050	-5.3%	41.2%	43.2%
Public Works (Engineering)	2,479,240	2,635,893	6.3%	5,421,184	5,770,952	6.5%	45.7%	45.7%
Finance and Administration	2,301,712	2,278,706	-1.0%	4,715,638	4,725,388	0.2%	48.8%	48.2%
Planning & Building	3,837,719	4,670,842	21.7%	8,492,888	8,477,058	-0.2%	45.2%	55.1%
Police	12,048,871	11,989,487	-0.5%	25,154,856	25,115,979	-0.2%	47.9%	47.7%
Fire	10,418,327	10,701,781	2.7%	20,286,014	20,932,948	3.2%	51.4%	51.1%
Total Expenditures	39,323,443	40,706,873	3.5%	83,534,621	83,209,548	-0.4%	47.1%	48.9%
Other Financing Uses:								
Interfund Transfers	2,039,391	2,024,568	-0.7%	8,480,717	5,430,801	-36.0%	24.0%	37.3%
Total Other Financing Uses	2,039,391	2,024,568	-0.7%	8,480,717	5,430,801	-36.0%	24.0%	37.3%
Total Expenditures & Other Uses	41,362,834	42,731,441	3.3%	92,015,338	88,640,349	-3.7%	45.0%	48.2%

*Budgeted and actual expenditures exclude working capital, operating reserves, and capital reserves.

Comparing 2016 and 2015 expenditures:

In 2016, excluding interfund transfers, General Fund expenditures were **3.5 percent higher** than 2015, and finished the second quarter at **48.9 percent of budget**. Specific reasons for increased expenditures are highlighted below:

- Expenditures for **Non-departmental** were **down 12.7 percent** due to the AT&T Mobility legal settlement payment early in 2015. Public Defender expenditures, which are newly charged to Non-departmental, offset a portion of the decrease. Non-departmental finished the second quarter at **38.7 percent of budget** spent.
- Actual 2016 expenditures for the **City Council increased 10.8 percent** from 2015. The increase is due to expenditures for the Community Survey, which is conducted in even-numbered years. City Council finished the quarter at **64.3 percent of budget**, which is normal as Membership Dues paid at the beginning of the year comprise a large portion of the overall budget.
- The **City Manager's Office** finished the second quarter **up 36.8 percent** from 2015 with **53.9 percent of budget** expended. The increase reflects the Deputy City Manager Reorganization, which occurred after the 1st quarter of 2015, and expenditures for the Police Strategic Plan.
- Second quarter expenditures for the **Parks & Community Services Department** were **down 0.9 percent** from 2015 due to an invoice for the Human Service Pooled Program, usually paid to Bellevue in the first quarter, which was paid early at the very end of 2015. Parks and Community Services finished the second quarter at **43.2 percent of budget**.

2016 General Fund actual expenditures (excluding "other financing uses") were 3.5 percent higher than they were in 2015.

Continued on page 5

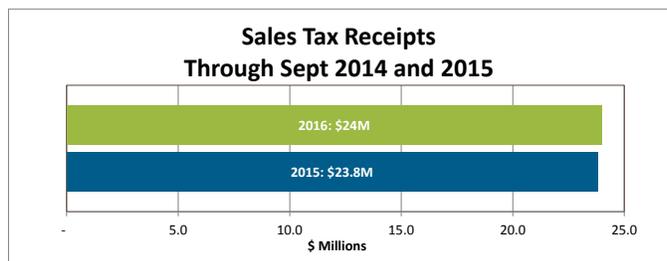
Financial Management Report as of June 30, 2016

- **Public Works - General Fund** expenditures were **6.3 percent above 2015**. Growth in expenditures in Wages and Benefits due to the addition of 4 positions for Capital Project Engineering was partially offset by decreased spending on Professional Services. Overall, Public Works - General Fund finished the first half of the year at **45.7 percent of budget**.
- **Planning and Building** finished the quarter **21.7 percent above 2015**, with **55.1 percent of the budget** expended. This is largely due to the addition of one-time and ongoing resources to meet workload demands associated with the high levels of development activity in Kirkland.
- **Police** expenditures ended the quarter **0.5 percent below 2015**, at **47.7 percent of budget**. This is consistent with performance in 2015.
- Expenditures for the **Fire Department** finished the first quarter **2.7 percent above 2015**. Fire finished the first half of 2016 at **51.1 percent of budget**. Expenses are within expected ranges, and similar to 2015 budget to actual performance. A greater proportion of fire overtime expenses come early in the year, as overtime expenditures to maintain minimum staffing over the winter holidays inflates these costs in January.
- Actual **Interfund Transfers** finished the second quarter **down 0.7 percent** from 2015 due to the offsetting impacts of a one time transfer from the Building and Property Reserve in 2015 more than offsetting the transfers for city hall construction debt service, which began in 2016.

Summary of Fire District 41 Funds	
Revenues & Expenditures	
Beginning Balance	5,230,000
Investment Interest	90,970
Expenditures:	114,893
Current Balance	\$ 5,206,077

Sales Tax Revenue Analysis

Sales tax revenue through the second quarter was **7.8 percent** higher in 2016 than 2015. This represents a slight deceleration in the growth rate from the 9.9 mark set in the first quarter. Increased activity in contracting, other retail, and services composed the bulk of the revenue gains. Sales tax revenue received through June is from sales activity between November 2015 and April 2016.



Review by business sectors:

- **Contracting** was **up 14.7 percent** through June compared to 2015. Construction collections continue to be strong this year, and lead overall sales tax growth. However, this is a very volatile revenue category.
- Sales tax from the retail sectors was collectively **up 4.6 percent** compared to 2015.
- **Auto/gas retail** sector was **up 3.6 percent** compared to 2015.
- **General merchandise/miscellaneous retail** sector was **down 3.0 percent** in 2016 compared to 2015 due to reduced revenue from major retailers.
- **Retail eating/drinking** sector performance was **up 4.5 percent** compared to 2015.
- **Other retail** was **up 13.3 percent** compared to 2015. Non store retail, which is the largest subcategory of this group, lead the growth in the first half of the year.
- The **services** sector was **up 6.8 percent** compared to 2015, largely due to growth in administrative support, health care and other services
- **Wholesale** revenues were **up 11.6 percent** in the first half of 2016. This sector is broken into durable and non-durable goods, both of which grew substantially.
- The **Miscellaneous** sector was **up 10.5 percent** through the first half of the year 2016, largely due to real estate and manufacturing growth.
- **Communications** grew 35.7 percent on the year. This is due to a one time refund that was paid to selected taxpayers in May of 2015.

Regional Sales Tax

Bellevue was up 8.7 percent, Redmond was up 51.2 percent through June 2016 compared to June 2015.

King County

King County's sales tax receipts were up 11.8 percent through the end of the quarter compared to 2015.

Business Sector Group	YTD		Dollar Change	Percent Change	Percent of Total	
	2015	2016			2015	2016
Services	1,225,077	1,308,548	83,471	6.8%	13.6%	13.5%
Contracting	1,333,581	1,529,295	195,714	14.7%	14.8%	15.8%
Communications	194,659	264,085	69,426	35.7%	2.2%	2.7%
Auto/Gas Retail	2,257,986	2,338,500	80,514	3.6%	25.1%	24.1%
Gen Merch/Misc Retail	1,060,691	1,029,243	(31,448)	-3.0%	11.8%	10.6%
Retail Eating/Drinking	731,752	764,561	32,809	4.5%	8.1%	7.9%
Other Retail	1,202,614	1,363,003	160,389	13.3%	13.4%	14.1%
Wholesale	458,127	511,243	53,116	11.6%	5.1%	5.3%
Miscellaneous	521,848	576,614	54,766	10.5%	5.8%	6.0%
Total	8,986,333	9,685,091	698,758	7.8%	100%	100%

Kirkland's sales tax base is comprised of a variety of businesses which are grouped and analyzed by business sector (according to "North American Industry Classification System" or NAICS).

Nine business sector groupings are used to compare 2015 and 2016 sales tax receipts in the table to the left.

Month	Sales Tax Receipts		Dollar Change	Percent Change
	2015	2016		
Jan	1,406,663	1,580,669	174,006	12.4%
Feb	1,783,689	1,958,877	175,188	9.8%
Apr	1,323,936	1,440,078	116,142	8.8%
May	1,599,980	1,675,944	75,964	4.7%
Jun	1,480,647	1,533,895	53,248	3.6%
Total	8,986,333	9,685,091	698,758	7.8%

When analyzing monthly sales tax receipts, there are two items of special note: First, most businesses remit their sales tax collections to the Washington State Department of Revenue on a monthly basis. Small businesses only have to remit their sales tax collections either quarterly or annually, which can create anomalies when comparing the same month between two years. Second, for those businesses which remit sales tax monthly, there is a two month lag from the time that sales tax is collected to the time it is distributed to the City.

- Sales tax revenues through the second quarter of 2016 were 7.8 percent higher than the secondquarter of 2015.
- Growth has slowed as the year has progressed. The first quarter was up 9.9 percent over 2015; April was up 9.6 percent, May was up 8.6 percent and June was up 7.8 percent. Though growth has slowed the outlook is still positive going forward.
- Aside from General Merchandise/Miscellaneous Retail, every sector grew in the second quarter. Contracting performed particularly well, followed by Other Retail and Services. These growth sectors, particularly Contracting, tend to be volatile and will fluctuate with changing economic conditions.
- General Merchandise is down 3.0 percent after the second quarter. General Merchandise decreased slightly from last year, though it is generally less volatile than other categories. This category is the most likely to contain impacts from the ongoing construction at Totem Lake and Kirkland Urban.

Kirkland's sales tax base is further broken down by business district (according to geographic area), as well as "unassigned or no district" for small businesses and businesses with no physical presence in Kirkland.

Comparing to the same period last year:

Totem Lake, which accounted for 28.7 percent of the total sales tax receipts in the second quarter, was **up 4.3 percent** from 2015 due to the continued sales growth in the automotive/gas retail sector and repairs & maintenance with mostly positive results in other sectors. Sixty percent of this business district's revenue comes from the auto/gas retail sector.

NE 85th Street, which made up 13.2 percent of the total sales tax receipts in 2016, was **up 3.8 percent** compared to 2015. This area's sales grew due to improving auto retail and retail eating/drinking sales. General retail, which is the second largest sector, fell 0.5 percent on the year. Auto and general retail contribute 81.7 percent of this business district's revenue.

Downtown, which accounted for 5.3 percent sales tax receipts through the second quarter, was **down 12.5 percent**. This is due to abnormally high revenues from the information category in 2015. If it wasn't for that anomaly, downtown revenues

would have fallen just 2.3 percent.

Carillon Point & Yarrow Bay, which account for 1.7 percent of the total sales tax receipts, were **up 0.2 percent** compared to 2015. About 62.1 percent of this business district's revenue came from retail eating/drinking and accommodations.

Houghton & Bridle Trails, which has produced 2.3 percent of the total sales tax receipts in 2016, were **up 3.8 percent** due to an increase in retail food stores and other retail, which offset a decrease in several other categories.

Juanita, which generated 1.4 percent of the total 2016 sales tax receipts, was **up 1.9 percent** compared to 2015. Increases in retail eating/drinking offset declines in several other sectors.

North Juanita, Kingsgate, & Finn Hill accounted for 2.6 percent of the total sales tax receipts in 2016 and were **up 1.1 percent** from 2015, with growth in North Juanita and Kingsgate offsetting a decline in Finn Hill. The former two grew by 1.9 and 3.6 percent, respectively, while the latter one declined by 5.3 percent. Finn Hill revenues declined across several sectors, however, the percentage decline only represents \$2,556.

Year-to-date tax receipts by business district for 2015 and 2016 are compared in the table on the next page.

Financial Management Report as of June 30, 2016

When reviewing sales tax receipts by business district, it's important to be aware that 48.8 percent of the revenues received in the second half of 2016 were in the "unassigned or no district" category largely due to contracting and other revenue, which includes revenue from internet, catalog sales and other businesses located outside of the City. This percentage has grown in recent years as internet sales have grown in volume.

Business District	YTD		Dollar Change	Percent Change	Percent of Total	
	2015	2016			2015	2016
Totem Lake	2,665,021	2,778,558	113,537	4.3%	29.7%	28.7%
NE 85th St	1,227,260	1,274,378	47,118	3.8%	13.7%	13.2%
Downtown	582,775	509,721	(73,054)	-12.5%	6.5%	5.3%
Carillon Pt/Yarrow Bay	166,926	167,253	327	0.2%	1.9%	1.7%
Houghton & Bridle Trails	212,468	220,610	8,142	3.8%	2.4%	2.3%
Juanita	128,363	130,858	2,495	1.9%	1.4%	1.4%
Kingsgate	78,360	81,215	2,855	3.6%	0.9%	0.8%
North Juanita	123,905	126,240	2,335	1.9%	1.4%	1.3%
Finn Hill	48,244	45,688	(2,556)	-5.3%	0.5%	0.5%
Unassigned or No District:						
Contracting	1,321,493	1,517,379	195,886	14.8%	14.7%	15.7%
Other	2,431,518	2,833,191	401,673	16.5%	31.1%	33.1%
Total	8,986,333	9,685,091	698,758	7.8%	100.0%	100.0%

Sales Tax Revenue Outlook After a fast start to 2016, revenue growth has steadily slowed through the second quarter. Year to date growth over the first half of the year has downshifted from a 9.9 percent pace in January to a 7.9 percent rate in June. The first quarter of 2015 was weak, so this is at least partially due to comparatively stronger prior year comparisons in the second quarter last year. Staff will continue to monitor and report on emerging trends in the monthly Sales Tax Report.

OFFICE VACANCIES:

According to the latest report from CB Richard Ellis Real Estate Services, Kirkland's office vacancy rate in the second quarter of 2016 was 3.6 percent, significantly lower than the Puget Sound total vacancy rate of 11.3 percent, though slightly higher than the first quarter's vacancy rate of 1.5 percent. Overall the Eastside is one of the stronger office markets in the Puget Sound region, with an office vacancy rate of 10.7 percent, just above downtown Seattle's vacancy rate of 9.5 percent.

The region currently has 6.5 million square feet of office space under construction, over 3.5 times more than this time last year. This includes projects on the Eastside, with over 1 million square feet planned in Bellevue.

LODGING TAX REVENUE:

Lodging tax revenue grew compared to 2015, finishing the quarter up 2.3 percent, an increase of \$2,653. This meant revenues finished the first quarter at 39.85 percent of budget.

Economic Environment Update The Washington State economy continued to expand, adding 20,200 nonfarm jobs since the February 2016 update, according to the Washington State Economic and Revenue Forecast Council. This was 2,8000 more than expected, lead by growth in the Construction sector.

The Conference Board's **Consumer Confidence Index** increased from 92.6 in May to 98.0 in June. A rating of 100 equals the 1985 consumer confidence level. This change was due to fewer negative feelings about current conditions relative to the past couple months, and a cautiously optimistic outlook for the near-term.

Unemployment Rates increased at the National level, up to 4.9 percent in June, from 4.7 percent in May. The unemployment rate in King County decreased from 4.4 percent in May to 4.3 percent in June, which is the latest available data point. King County unemployment rates fell from 5.1 percent in January and have remained between 4.1 and 4.6 percent since March.

The Western Washington Purchasing Manager Index indicated stalled growth in economic activity in June 2016. The index was at 49.2 in June; an index reading greater than 50 signals an expanding economy. While the index shows stagnation, it is an improvement of 1.1 points over May's reading.

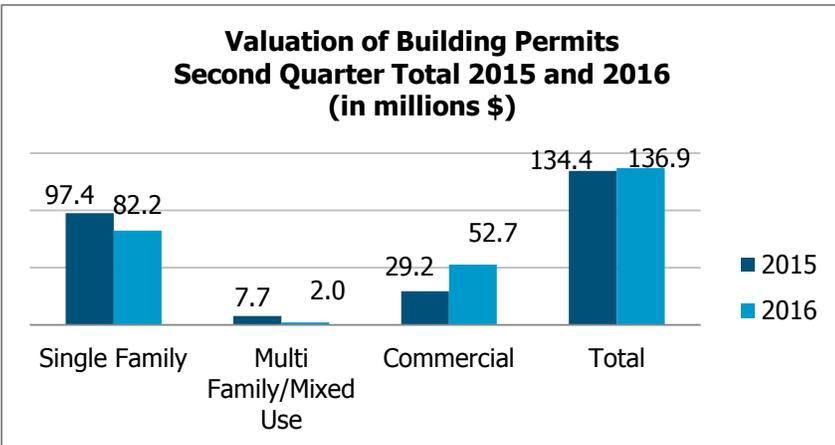
(Continued on page 8)

Economic Environment Update *continued*

Local **building permitting activity** has increased 1.8 percent compared to June 2015. The increase is due entirely to commercial development, which is up 80.2 percent from this time last year. Totem Lake and Kirkland Urban development are driving this increase. For as much as commercial development increased, single family and multi-family/mixed use development fell almost as much, declining 15.7 and 74.2 percent respectively. The net effect is a year-to-date growth of just \$2.5 million in development valuation.

Prices in the **housing market** continued to increase in the second quarter of 2016 with the Case-Shiller housing index for the Seattle metro area up to 202.58, increasing the gap above the pre-recession peak index score of 192.3 set in July 2007. There were 42,600 new housing permits issued in the second quarter of 2016 according to the Washington State Economic and Revenue Council.

Inflation in the Seattle area is high relative to the national rate. In June 2016, the Seattle core CPI increased 2.0 percent compared to the previous year, while the national CPI was at 0.6 percent year-to-year growth.



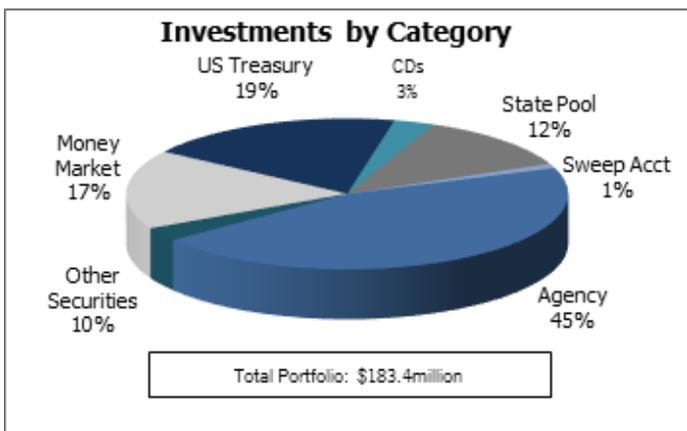
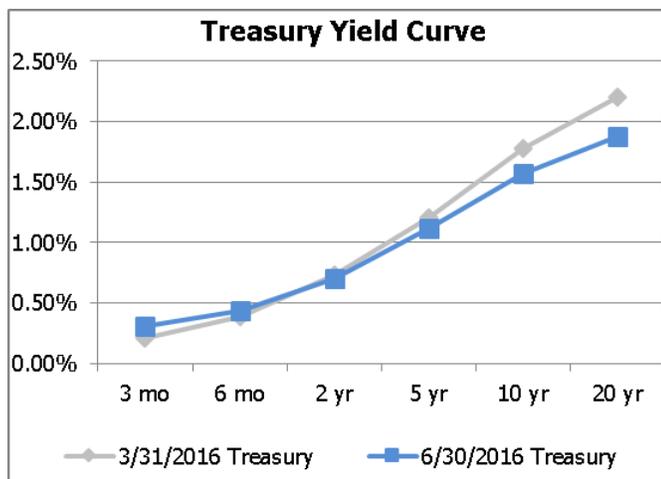
Investment Report

MARKET OVERVIEW

The mild economic growth continued to slow down into the 2nd quarter of 2016. The Fed Funds rate increase expectations which started the year with four expected ¼ percent increases are now at one expected ¼ percent increase in 2016. The more likely scenario is that there will be no rate increases for the remainder of this year. The yield curve rose on the short end of the curve and fell at the long end, flattening the curve slightly, as seen in the graph below.

place an undue financial burden on the City.

The City's portfolio increased \$15.8 million in the 2nd quarter of 2016, moving from \$167.6 million on March 31, 2016 to \$183.4 million on June 30, 2016. The increase in the portfolio is related, in part, to the normal cash flows of the 2nd quarter, as the first half of property taxes is received at the end of April and early May.



CITY PORTFOLIO

The primary objectives for the City of Kirkland's investment activities are: legality, safety, liquidity and yield. Additionally, the City diversifies its investments according to established maximum allowable exposure limits so that reliance on any one issuer will not

Diversification

The City's current investment portfolio is composed of Government Sponsored Enterprises (GSEs) bonds, US Government Obligations, State and Local Government bonds, Bank CDs, Money Market Account and the State Investment Pool. City investment procedures allow for 100% of the portfolio to be invested in U.S. Treasury or Federal Government obligations.

Financial Management Report as of June 30, 2016

2016 ECONOMIC

OUTLOOK and

INVESTMENT STRATEGY

While the outlook for growth in the U.S. economy looks weaker now than it did three months ago, it is projected to continue growing at the slower pace. The U.S. economy is expected to grow at an annual rate of 1.5 percent in 2016 and 2.3 percent in 2017. CPI inflation is expected to average 1.6 percent in 2016 and 2.3 percent in 2017. The unemployment rate is expected to average 4.8 percent in 2016 and fall to 4.6 percent in 2017. The Fed Funds rate, currently at 0.50%, is expected to rise one time in late 2016 to 0.75%.

The City's investment advisor, Government Portfolio Advisors (GPA) is currently recommending that the duration of the portfolio be increased slightly in relation to the benchmark. They believe that the Fed may be slow to raise Fed Funds and will recommend security purchases when opportunities to capture higher returns are available.

The State Pool is currently at 0.51%, slowly rising each month as shorter term rates increase. However, rates will continue to remain low as the Fed Funds rate remains at 0.25 to 0.50 percent. Total estimated investment income for 2016 is \$1,200,000.

Investment Report *continued*

Liquidity

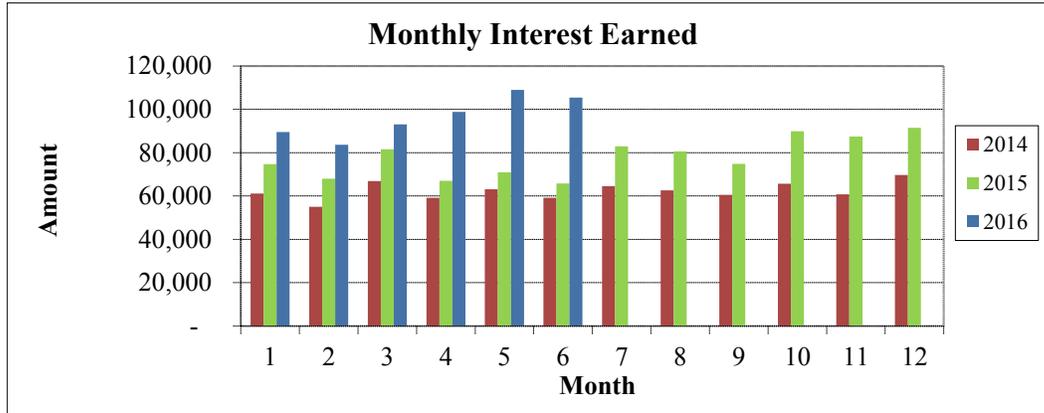
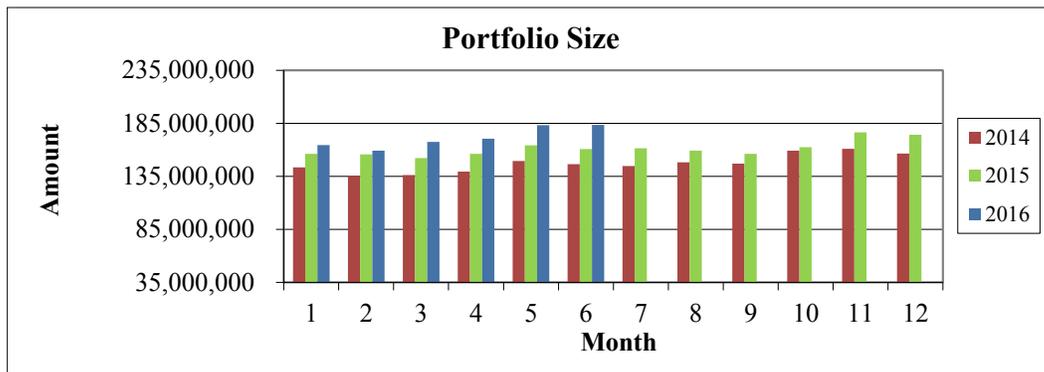
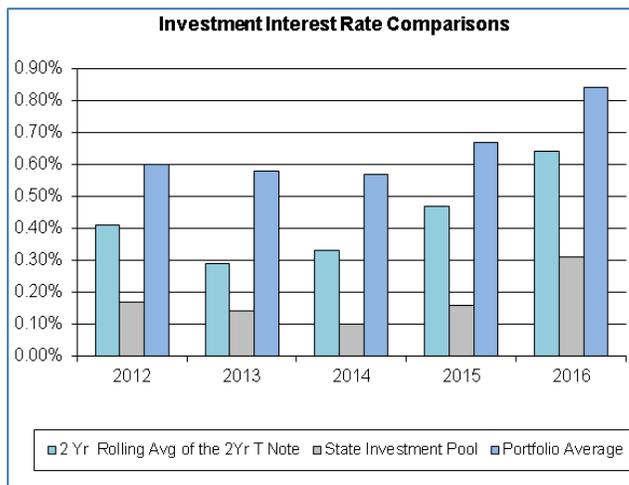
The target duration for the City's portfolio is based on the 0-5 year U.S. Treasury. The average maturity of the City's investment portfolio decreased from 1.42 years on March 31, 2016 to 1.38 years on June 30, 2016 as securities were called.

Yield

The City Portfolio yield to maturity increased from 0.85 percent on March 31, 2016 to 0.91 percent on June 30, 2016. Through June 30, 2016, the City's annual average yield to maturity also increased to 0.84 percent. The City's portfolio benchmark is the range between the 90 day Treasury Bill and the 2 year rolling average of the 2 year Treasury Note. This benchmark is used as it is reflective of the maturity guidelines required in the Investment Policy adopted by City Council.

The City's portfolio outperformed both the 90 day T Bill and the 2 year rolling average of the 2 year Treasury note, which was 0.67 percent on June 30, 2016.

The City's implementation of a more active investment strategy due to contracting with an investment advisor has resulted in increasing portfolio yields. The City's portfolio's rate of return is rising with the rise in interest rates and is keeping ahead of the benchmark rates as seen in the adjacent graph.



Reserves are an important indicator of the City's fiscal health and effectively represent "savings accounts" that are established to meet unforeseen budgetary needs (general purpose reserves) or are dedicated to a specific purpose. Ending balances in the table below are based on budget. Actual balances in some reserves may vary based on revenue performance (e.g., Excise Tax and Impact Fees).

Reserve Analysis

- Positive General Fund performance in 2013-2014, along with planned contributions to reserves in 2015-2016 has allowed the City to plan to replenish many of the general purpose reserves to target levels by the end of 2016 as indicated in the table below. The City's fiscal policy is to set at least 1 percent of the General Fund adopted budget toward reserve replenishment toward 80 percent of the target level (100 percent for the Revenue Stabilization Reserve). Unplanned amounts available at the end of a biennium should help replenish to target faster, which is what happened at the end of 2014. Adequate fund balance and reserve levels are a necessary component of financial management strategy and a key factor in the external agencies' measurement of the City's financial strength (Standard and Poor's: AAA and Moody's Aa2).

General Capital Reserves

- Real estate activity has been growing significantly over the last few years and 2015 reached an all-time high in **Real Estate Excise Tax (REET)** collections. However, **2015 is 19.2 percent ahead of second quarter 2015**. The current ending balances do not reflect this revenue performance, however they do incorporate 2015-2016 uses in the 2015-2020 Capital Improvement Plan as adopted in December 2015.
- Impact fees (Parks and Transportation)** are a reflection of development activity, which remains strong. However, 2016 Park revenue is 55.8% behind 2015 due to revenue received from a single large development in the first quarter of 2015. Normalizing for this event, revenue is only slightly down from last year. Transportation is 3.1 percent ahead. There are large developments underway which are expected to generate significant fees in 2016 that likely will bring these revenues in line with last year. The balances below were adjusted during the 2015-2020 CIP adoption in December to fund capital projects that are budgeted during this biennium.
- The City adopted a new Capital Improvement Program (CIP) for 2015-2020, which made significant uses of REET and Impact Fees in the current budget period, as well as future years in response to projects identified in several long-range master plans that were adopted in 2015.

General Government & Utility Reserves Targets Summary

Reserves	Actual 2015 Beginning Balance	Adopted 2016 Ending Balance	Revised 2016 Ending Balance	2015-16 Target	Revised Over (Under) Target
GENERAL PURPOSE RESERVES WITH TARGETS					
General Fund Reserves:					
General Fund Contingency	50,000	50,000	50,000	50,000	-
General Oper. Reserve (Rainy Day)	2,806,513	4,803,388	4,803,388	4,803,388	-
Revenue Stabilization Reserve	2,570,090	2,848,220	2,848,220	2,848,220	-
Building & Property Reserve	571,579	600,000	533,000	600,000	(67,000)
Council Special Projects Reserve	250,000	250,000	134,000	250,000	(116,000)
Contingency	2,426,425	4,036,425	4,036,425	5,512,218	(1,475,793)
General Capital Contingency	3,768,012	4,961,855	4,961,855	5,701,001	(739,146)
General Purpose Reserves with Targets	12,442,619	17,549,888	17,366,888	19,764,827	(2,397,939)
ALL OTHER RESERVES WITH TARGETS					
General Fund Reserves:					
Litigation Reserve	150,000	150,000	150,000	150,000	-
Firefighter's Pension Reserve	1,493,687	1,225,835	1,225,835	933,405	292,430
Health Benefits Fund:					
Claims Reserve	2,058,311	2,058,311	2,058,311	2,058,311	-
Rate Stabilization Reserve	1,000,000	1,000,000	1,000,000	1,000,000	-
Excise Tax Capital Improvement:					
REET 1	5,843,876	8,697,813	5,213,854	1,732,329	3,481,525
REET 2	4,888,788	7,146,044	6,000,344	2,436,255	3,564,089
Water/Sewer Operating Reserve:					
Water/Sewer Operating Reserve:	2,414,471	2,659,932	2,659,932	2,659,932	-
Water/Sewer Capital Contingency:	1,107,600	613,300	613,300	613,300	-
Surface Water Operating Reserve:	706,364	893,306	893,306	893,306	-
Surface Water Capital Contingency:	845,163	391,380	391,380	391,380	-
Other Reserves with Targets	20,508,260	24,835,921	20,206,262	12,868,218	7,338,044
Reserves without Targets	44,926,198	58,197,292	48,308,247	n/a	n/a
Total Reserves	77,877,077	100,583,101	85,881,397	n/a	n/a

The target comparison reflects revised ending balances to the targets established in the budget process for those reserves with targets.

General Purpose reserves are funded from general revenue and may be used for any general government function.

All Other Reserves with Targets have restrictions for use either from the funding source or by Council-directed policy (such as the Litigation Reserve).

The summary to the right details all Council authorized uses and additions in the 2015-16 biennium.

USES AND ADDITIONS HIGHLIGHTS

RESERVE	AMOUNT	DESCRIPTION
2015-16 Council Authorized Uses		
Prior 2015-2016 Uses	\$14,679,281	
Building & Property Reserve	\$67,000	CKC Property Acquisition from BNSF
Council Special Projects	\$30,000	Kirkland Community Foundation
Tour Dock Reserve	\$21,500	Port of Seattle Economic Development Partnership
2015-16 Council Authorized Additions		
Prior 2015 Additions	\$96,077	

General Fund and Contingency reserves are funded from general purpose revenue and are governed by Council-adopted policies.

Special Purpose reserves reflect both restricted and dedicated revenue for specific purpose, as well as general revenue set aside for specific purposes.

General Capital Reserves provide the City the ability to respond to unexpected changes in costs and accumulate funds for future projects. It is funded from both general revenue and restricted revenue.

Utility reserves are funded from utility rates and provide the utilities with the ability to respond to unexpected costs and accumulate funds for future replacement projects.

Internal service funds are funded by charges to operating departments. They provide for the accumulation of funds for replacement of equipment, as well as the ability to respond to unexpected costs.

Reserves		Est. 2015	Adopted	Additional	Revised
Description		Beginning	2016 Ending	Authorized	2016 Ending
		Balance	Balance*	Uses/Additions	Balance
GENERAL FUND/CONTINGENCY					
General Fund Reserves:					
General Fund Contingency	Unexpected General Fund expenditures	50,000	50,000		50,000
General Oper. (Rainy Day)	Unforeseen revenues/temporary events	2,806,513	4,803,388		4,803,388
Revenue Stabilization	Temporary revenue shortfalls	2,570,090	2,848,220		2,848,220
Building & Property	Property-related transactions	571,579	600,000	(67,000)	533,000
Council Special Projects	One-time special projects	250,000	250,000	(116,000)	134,000
Contingency	Unforeseen expenditures	2,426,425	4,036,425		4,036,425
Total General Fund/Contingency		8,674,607	12,588,033	(183,000)	12,405,033
SPECIAL PURPOSE RESERVES					
General Fund Reserves:					
Litigation	Outside counsel costs contingency	150,000	150,000		150,000
Labor Relations	Labor negotiation costs contingency	74,928	55,312		55,312
Police Equipment	Equipment funded from seized property	50,284	75,969		75,969
Fire OT & Equipment	Contingency for overtime and equipment	200,000	200,000		200,000
LEOFF 1 Police	Police long-term care benefits	618,079	618,079		618,079
Facilities Expansion	Special facilities expansions	150,982	50,663		50,663
Development Services	Revenue and staffing stabilization	2,572,520	2,612,670		2,612,670
Development Svcs. Technology	Permit system replacement	1,040,324	1,356,175		1,356,175
Tour Dock	Dock repairs	206,271	273,095	(21,500)	251,595
Tree Ordinance	Replacement trees program	56,267	65,488		65,488
Revolving/Donation Accounts	Fees/Donations for specific purposes	940,331	943,300	(25,000)	918,300
Lodging Tax Fund	Tourism program and facilities	310,420	190,548	(119,549)	70,999
Cemetery Improvement	Cemetery improvements/debt service	736,215	767,040	2,568	769,608
Off-Street Parking	Downtown parking improvements	259,161	391,613	(285,500)	106,113
Fire Equipment Life Cycle	20-year fire equipment costs	418,326	896,704		896,704
Police Equipment Life Cycle	20-year police equipment costs	343,114	806,243		806,243
Technology Equipment Life Cycle	20-year technology equipment costs	663,600	1,265,117		1,265,117
Firefighter's Pension	Long-term care/pension benefits	1,493,687	1,225,835		1,225,835
Total Special Purpose Reserves		10,284,509	11,943,851	(448,981)	11,494,870
GENERAL CAPITAL RESERVES					
Excise Tax Capital Improvement:					
REET 1	Parks/transportation/facilities projects, parks debt service	5,843,876	8,697,813	(3,483,959)	5,213,854
REET 2	Transportation and other capital projects	4,888,788	7,146,044	(1,145,700)	6,000,344
Impact Fees					
Transportation	Transportation capacity projects	3,663,839	4,227,671	(2,300,900)	1,926,771
Parks	Parks capacity projects	1,727,746	2,007,936	(484,599)	1,523,337
Street Improvement	Street improvements	995,958	995,958	(995,958)	0
General Capital Contingency	Changes to General capital projects	3,768,012	4,961,855		4,961,855
Total General Capital Reserves		20,888,219	28,037,277	(8,411,116)	19,626,161
UTILITY RESERVES					
Water/Sewer Utility:					
Water/Sewer Operating	Operating contingency	2,414,471	2,659,932		2,659,932
Water/Sewer Debt Service	Debt service	498,591	495,390	(460,000)	35,390
Water/Sewer Capital Contingency	Changes to Water/Sewer capital projects	1,107,600	613,300		613,300
Water/Sewer Construction	Replacement/re-prioritized/new projects	10,051,937	17,664,869	(4,127,036)	13,537,833
Surface Water Utility:					
Surface Water Operating	Operating contingency	706,364	893,306		893,306
Surface Water Capital Contingency	Changes to Surface Water capital projects	845,163	391,380		391,380
Surface Water Construction	Trans. related surface water projects	5,656,579	7,597,175	(759,300)	6,837,875
Total Utility Reserves		21,280,705	30,315,352	(5,346,336)	24,969,016
INTERNAL SERVICE FUND RESERVES					
Health Benefits:					
Claims	Health benefits self insurance claims	2,058,311	2,058,311		2,058,311
Rate Stabilization	Rate stabilization	1,000,000	1,000,000		1,000,000
Equipment Rental:					
Vehicle	Vehicle replacements	10,068,738	8,583,511	22,829	8,606,340
Radio	Radio replacements	59,463	74,764		74,764
Information Technology:					
PC Replacement	PC equipment replacements	459,063	518,292		518,292
Major Systems Replacement	Major technology systems replacement	656,200	1,165,089	135,200	1,300,289
Facilities Maintenance:					
Operating	Unforeseen operating costs	550,000	550,000		550,000
Facilities Sinking Fund	20-year facility life cycle costs	1,897,262	3,748,621	(470,300)	3,278,321
Total Internal Service Fund Reserves		16,749,037	17,698,588	(312,271)	17,386,317
Grand Total		77,877,077	100,583,101	(14,701,704)	85,881,397

*Adjusted for actual cash balances in April



The Financial Management Report (FMR) is a high-level status report on the City's financial condition that is produced quarterly.

- It provides a **summary budget to actual and year over year comparisons** for year-to-date revenues and expenditures for all operating funds.
 - The **Sales Tax Revenue Analysis** report takes a closer look at one of the City's larger and most economically sensitive revenue sources.
 - **Economic environment** information provides a brief outlook at the key economic indicators for the Eastside and Kirkland such as office vacancies, residential housing prices/sales, development activity, inflation and unemployment.
 - The **Investment Summary** report includes a brief market overview, a snapshot of the City's investment portfolio, and the City's year-to-date investment performance.
 - The **Reserve Summary** report highlights the uses of and additions to the City's reserves in the current year as well as the projected ending reserve balance relative to each reserve's target amount.
- Tracey Dunlap, Deputy City Manager
 - Michael Olson, Director of Finance & Administration
 - Tom Mikesell, Financial Planning Manager
 - Neil Kruse, Senior Financial Analyst
 - George Dugdale, Senior Financial Analyst
 - Kyle Butler, Budget Analyst
 - Elijah Panci, Budget Analyst



City of Kirkland
123 5th Avenue
Kirkland, WA 98033
Ph. 425-587-3146

Economic Environment Update References:

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- S&P/Case-Shiller Seattle Home Price Index
- U.S. Bureau of Labor Statistics
- Washington State Employment Security Department
- Washington State Department of Revenue
- Washington State Department of Labor & Industries
- City of Kirkland Building Division
- City of Kirkland Finance & Administration Department