



**CITY OF KIRKLAND**  
**Department of Finance & Administration**  
123 Fifth Avenue, Kirkland, WA 98033 425.587.3100  
[www.ci.kirkland.wa.us](http://www.ci.kirkland.wa.us)

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## **MEMORANDUM**

**To:** Dave Ramsay, City Manager

**From:** Tracey Dunlap, Director of Finance and Administration  
Sandi Miller, Financial Planning Manager

**Date:** September 8, 2006

**Subject:** Public Hearing on Revenue Sources for the 2007-2008 Budget

### **RECOMMENDATION:**

City Council hold a public hearing on September 19, 2006 on revenue sources for the 2007-2008 Budget.

### **BACKGROUND:**

This is the first of two required public hearings on the budget. The second public hearing on the 2007-2008 Preliminary Budget will be held on November 21<sup>st</sup>.

### **General Fund Forecast**

The City Council began their discussion of the 2007-2008 Budget at their mid-year budget review meeting held on June 15, 2006. At that time staff projected a General Fund deficit of \$418,000 in 2007 and \$1,539,000 in 2008 given the following revenue assumptions:

- 1% optional property tax taken in 2007 and 2008
- 2% annual growth in new construction (property tax)
- Sales tax lag of 1 year for 2007 – 2012
- 6% annual growth in sales tax
- 4% annual growth in utility taxes
- 2% annual growth in other taxes (including the revenue generating regulatory license)
- 5% annual growth in other revenues
- EMS levy maintained

The financial planning staff is currently engaged in balancing each operating fund's basic budget for 2007-2008. Though things are still in a state of flux, it appears that the strong growth in sales tax and development-related fees will help to close the projected General Fund deficit of \$418,000 in 2007, although it is important to note that those revenue categories are cyclical in nature. However, a deficit is still projected for 2008 that will need to be addressed.

The General Fund Revenue Summary from the April 2006 Financial Management Report is included as Attachment A for reference as to the status of revenues in 2006.

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One item that is expected to be discussed as part of the 2007-08 budget process is the potential impact of the pending Washington Supreme Court review of the constitutionality of Initiative 747. To provide an introduction to this issue, the summary contained in the "Budget Suggestions for 2007" published by MRSC in August 2006 is included as Attachment B.

### **Public Information and Process**

In addition to the public hearing, information about the budget will be posted on the City's web page and an article will be prepared for the City Update.

Upcoming, significant dates in the budget process include the following:

- October 9<sup>th</sup>: Finance Committee review of budget issues and process
- October 20<sup>th</sup>: Submit 2007-2008 Preliminary Budget to the City Council
- November 2<sup>nd</sup>: First study session on budget
- November 8<sup>th</sup> & 9<sup>th</sup>: Additional study sessions on budget (tentative)
- November 21<sup>st</sup>: Second public hearing on the Preliminary 2007-2008 Budget as amended by the Council
- December Council Meeting (TBD): Anticipated date for adoption of budget and property tax levy

**CITY OF KIRKLAND**  
**RESOURCE REPORT: GENERAL FUND**  
**For the Period Ending April 30, 2006**

Resource Category	2006 Budgeted Revenues*	2006 Actual Revenues*	Amount Over/(Under) Budget	% of Budget	Target
<b>Taxes:</b>					
Retail Sales Tax: General	12,392,069	4,868,387	(7,523,682)	39.3%	33.0%
Retail Sales Tax: Criminal Justice	890,000	330,515	(559,485)	37.1%	33.0%
Property Tax	8,117,113	2,127,444	(5,989,669)	26.2%	25.0%
Utility Taxes	7,171,200	2,868,004	(4,303,196)	40.0%	35.0%
Rev Generating Regulatory License	900,000	357,466	(542,534)	39.7%	40.0%
Other Taxes	464,800	172,294	(292,506)	37.1%	33.0%
<b>Total Taxes</b>	<b>29,935,182</b>	<b>10,724,110</b>	<b>(19,211,072)</b>	<b>35.8%</b>	<b>33.0%</b>
<b>Licenses &amp; Permits:</b>					
Building, Structural & Equipment Permits	1,850,742	867,076	(983,666)	46.9%	33.0%
Business Licenses/Franchise Fees	1,184,775	570,054	(614,721)	48.1%	40.0%
Other Licenses & Permits	128,020	44,803	(83,217)	35.0%	33.0%
<b>Total Licenses &amp; Permits</b>	<b>3,163,537</b>	<b>1,481,933</b>	<b>(1,681,604)</b>	<b>46.8%</b>	<b>33.0%</b>
<b>Intergovernmental:</b>					
Grants	88,693	41,868	(46,825)	47.2%	N/A
State Shared Revenues & Entitlements	581,780	194,239	(387,541)	33.4%	40.0%
Fire District #41	3,141,052	0	(3,141,052)	0.0%	0.0%
EMS	489,685	0	(489,685)	0.0%	0.0%
Other Intergovernmental Services	438,539	331,987	(106,552)	75.7%	N/A
<b>Total Intergovernmental</b>	<b>4,739,749</b>	<b>568,094</b>	<b>(4,171,655)</b>	<b>12.0%</b>	<b>15.0%</b>
<b>Charges for Services:</b>					
Internal Charges	3,531,586	1,098,759	(2,432,827)	31.1%	30.0%
Engineering Services	400,000	180,871	(219,129)	45.2%	33.0%
Plan Check & Development Fees	2,021,836	562,316	(1,459,520)	27.8%	33.0%
Recreation	74,000	12,150	(61,850)	16.4%	20.0%
Other Charges for Services	599,898	145,200	(454,698)	24.2%	25.0%
<b>Total Charges for Services</b>	<b>6,627,320</b>	<b>1,999,296</b>	<b>(4,628,024)</b>	<b>30.2%</b>	<b>30.0%</b>
<b>Fines &amp; Forfeits</b>	<b>1,157,550</b>	<b>267,908</b>	<b>(889,642)</b>	<b>23.1%</b>	<b>25.0%</b>
<b>Miscellaneous</b>	<b>585,814</b>	<b>98,033</b>	<b>(487,781)</b>	<b>16.7%</b>	<b>N/A</b>
<b>Total Revenues</b>	<b>46,209,152</b>	<b>15,139,374</b>	<b>(31,069,778)</b>	<b>32.8%</b>	<b>30.0%</b>
<b>Other Financing Sources:</b>					
Interfund Transfers	301,244	0	(301,244)	0.0%	N/A
<b>Total Other Financing Sources</b>	<b>301,244</b>	<b>0</b>	<b>(301,244)</b>	<b>0.0%</b>	<b>N/A</b>
<b>Total Resources</b>	<b>46,510,396</b>	<b>15,139,374</b>	<b>(31,371,022)</b>	<b>32.6%</b>	<b>N/A</b>

\* Budgeted and actual revenues exclude resources forward.

## I-747 Declared Unconstitutional

On June 13, 2006, Judge Mary Roberts ruled in King County Superior Court that Initiative 747, passed in November 2001, was unconstitutional. That initiative, as written, told voters that the amount that taxing jurisdictions could increase their property tax levy without a vote of the people would fall from two percent to one percent, if passed. However, the two percent limit from the passage of Initiative 722 (which reduced the increase in the levy limit from six to two percent) had been declared unconstitutional before Initiative 747 went to the voters.

Judge Roberts ruled that the voters in November 2001 were misled.

When I-747 went to the voters on November 6, 2001, the voters were incorrectly led to believe they were voting to amend I-722. They were incorrectly led to believe they were voting on a change in the tax increase cap from two percent to one percent. Instead, they were voting on a change from six percent to one percent. The voters were misled as to the nature and content of the law to be amended, and the effect of the amendment upon it. The constitution forbids this.

She also enjoined the state from enforcing any of the provisions of I-747, which means the law is back to what was prior to November 2001. However, local jurisdictions should use caution in taking any action in reliance on the lower court decision.

Since the time of this ruling, Attorney General Rob McKenna has said that the state will be appealing the ruling to the Washington State Supreme Court. He has also stated the he will seek a “stay,” which means that if it is granted, the maximum levy increase would remain at one percent – the I-747 limit – until the supreme court has ruled.

The governor and various legislators have also spoken out since the ruling came down. They will be looking at the “limit factor” during the 2007 legislative session and there could be legislation that would result in it being something different than six percent or one percent.

*Q: What does this mean for our levy of taxes for 2007?*

A: If a stay is granted or if there is a Supreme Court ruling by November 30, 2006, reversing the lower court decision, the maximum allowable increase will be the amount allowed by I-747 – one percent.

Assuming that there is no court decision by November 30, 2006 and no stay granted for the King County ruling, the levy increase limits in effect will be six percent for jurisdictions with a population under 10,000.

For jurisdictions with a population of 10,000 or more, the allowed increase will be the lesser of six percent or the increase in the implicit price deflator for personal consumption expenditures (IPD) for July as reported in the September issue of the *Survey of Current Business*. The lesser amount will surely be the IPD, given the information we have on it so far. (See page 15.) Those jurisdictions, however, have the opportunity to pass an ordinance or resolution making a finding of “substantial need” that would allow them to go to six percent.

Note, however, that if a supreme court decision after November 30, 2006 reverses the lower court ruling and finds that I-747 is constitutional or if the legislature in 2007 amends RCW 84.55.005 to specify some “limit factor” less than six percent, any jurisdiction that raised its levy by more than the new allowable amount may

have to refund the difference and also bear the costs of making the refund. Local governments should also be aware that any actions this year may have political consequences or impact future legislation and possible initiatives.

*Q: I have heard that the Department of Revenue says we may be able to levy banked capacity we missed out on because of the one percent limit of I-776 in past years? Is that true?*

Yes, in the June 2006 issue of *Property Tax Review*,<sup>1</sup> Peri Maxi, the retiring assistant director of the Property Tax Division, wrote:

A preliminary legal analysis suggests that local taxing districts may be able to increase their tax levies by up to six percent in 2007, plus a certain amount of “banked capacity” that would be the difference between the 1 percent increase in taxes they levied under I-747 and what they could have levied under Referendum 47. For smaller districts this would be the difference between 1 percent and 6 percent, but for districts with populations of 10,000 or more, it would be the difference between 1 percent and the Implicit Price Deflator (IPD) a measure of inflation that averaged about 2 percent from 2002 through 2006.

From what we have heard, King County is presently calculating what the banked capacity would have been. We don't know about other counties. But, the same admonition given above holds. If a jurisdiction does a property tax levy for 2007 using banked capacity resulting from the recalculation, it still might have to refund the money. Banked capacity from years preceding the passage of I-747 or from legislative body decisions since its passage to increase levies by less than one percent are not affected by the current events.

*Q: Can we do something to bank capacity for 2007?*

A: We have been told by the Department of Revenue (DOR) that the following will happen if there has been no supreme court ruling reversing the superior court decision and/or if no stay of the superior court ruling has been granted by November 30, 2006.

If your jurisdiction has a population of less than 10,000, you will automatically have the difference between what you levy (one percent is safest) and six percent “banked” if you have complied with the requirement in RCW 84.55.120 to pass a resolution or ordinance stating your levy increase over the prior year in dollar and percentage amounts. (Of course, this increase must not push your tax rate over the maximum allowed.) This is nothing new. You have been required to pass this resolution this since the passage of Referendum 47 in 1997.

If your population is 10,000 or more, you should pass a resolution or ordinance making a finding of “future substantial need” for the difference between what you choose to levy (one percent is safest) and six percent, assuming that this does not require an increase in your tax rate above the statutory maximum. This resolution or ordinance would be in addition to your property tax levy ordinance and your resolution or ordinance to be in compliance with RCW 84.55.120, stating your levy increase in percentage or dollar amounts.

This would put you in a “wait and see” position. You would not be passing a levy for 2007 that could be reduced by a court ruling or legislative action and require you to amend your budget. But, you would be reserving this levy capacity for a future year if it turns out that it is possible to do that. This is the safest and most conservative thing to do.

*Q: We have been thinking of doing a levy lid lift. How does this ruling on I-747 affect that?*

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<sup>1</sup>[http://dor.wa.gov/Docs/Pubs/Prop\\_Tax/NewsletterSummer2006.pdf](http://dor.wa.gov/Docs/Pubs/Prop_Tax/NewsletterSummer2006.pdf)

While there is a scenario that might make such a lid lift unnecessary, we would suggest you continue with your plans. There is nothing in the ruling on I-747 that affects levy lid lifts.