



**CITY OF KIRKLAND**  
**Department of Finance & Administration**  
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**MEMORANDUM**

**To:** Kurt Triplett, City Manager

**From:** Michael Olson, Director of Finance & Administration  
 Chip Corder, Temporary 2021-2022 Budget Development Staff  
 Robby Perkins-High, Senior Financial Analyst  
 Kevin Lowe Pelstring, Budget Analyst

**Date:** September 18, 2020

**Subject:** August 2020 Sales Tax Revenue

**Background**

The Financial Planning Division prepares a monthly sales tax revenue memo analyzing monthly and year-to-date activity by business sector, forecasting sales tax revenue in the current year, and tracking key economic indicators to provide additional context for the state of the economy. The general retail sales tax is the City's largest single revenue source, accounting for 19 percent of total budgeted revenues in the General Fund and funding, along with property tax and utility taxes, public safety and other general government (i.e., non-utility) services. It is also more sensitive to economic cycles than other tax revenues. Accordingly, it is monitored closely by staff—even more so given the economic disruption and uncertainty caused by COVID-19.

There is a two-month lag between when sales tax is generated and when it is distributed to the City by the Washington State Department of Revenue (DOR). Accordingly, August sales tax revenue relates to June retail activity in Kirkland.

**August 2020 vs. August 2019**

Business Sector Group	August		Dollar Change	Percent Change	Percent of Total	
	2019	2020			2019	2020
Services	355,452	359,661	4,209	1.2%	13.5%	15.2%
Contracting	755,850	633,999	(121,851)	-16.1%	28.7%	26.8%
Communications	36,880	37,771	891	2.4%	1.4%	1.6%
Retail:						
Auto/Gas Retail	545,916	424,668	(121,248)	-22.2%	20.8%	18.0%
Gen Merch/Misc Retail	221,646	243,013	21,367	9.6%	8.4%	10.3%
Retail Eating/Drinking	179,270	132,101	(47,169)	-26.3%	6.8%	5.6%
Other Retail	279,623	285,847	6,224	2.2%	10.6%	12.1%
Wholesale	104,498	127,200	22,702	21.7%	4.0%	5.4%
Miscellaneous	152,866	119,516	(33,350)	-21.8%	5.8%	5.0%
<b>Total</b>	<b>2,632,001</b>	<b>2,363,776</b>	<b>(268,225)</b>	<b>-10.2%</b>	<b>100%</b>	<b>100%</b>

**Comparing August 2020 to August 2019, sales tax revenue is down \$268,225 (10.2 percent).**

Looking at business sectors, **the most significant growth occurred in Wholesale (up \$22,702, or 21.7 percent) and General Merchandise/Miscellaneous Retail (up \$21,367, or 9.6 percent).**

**Noteworthy declines occurred in Contracting (down \$121,851, or 16.1 percent), Auto/Gas Retail (down \$121,248, or 22.2 percent), Retail Eating/Drinking (down \$47,169, or 26.3 percent), and Miscellaneous (down \$33,350, or 21.8 percent),** which primarily encompasses finance & insurance, real estate, and manufacturing.

#### YTD 2020 vs. YTD 2019

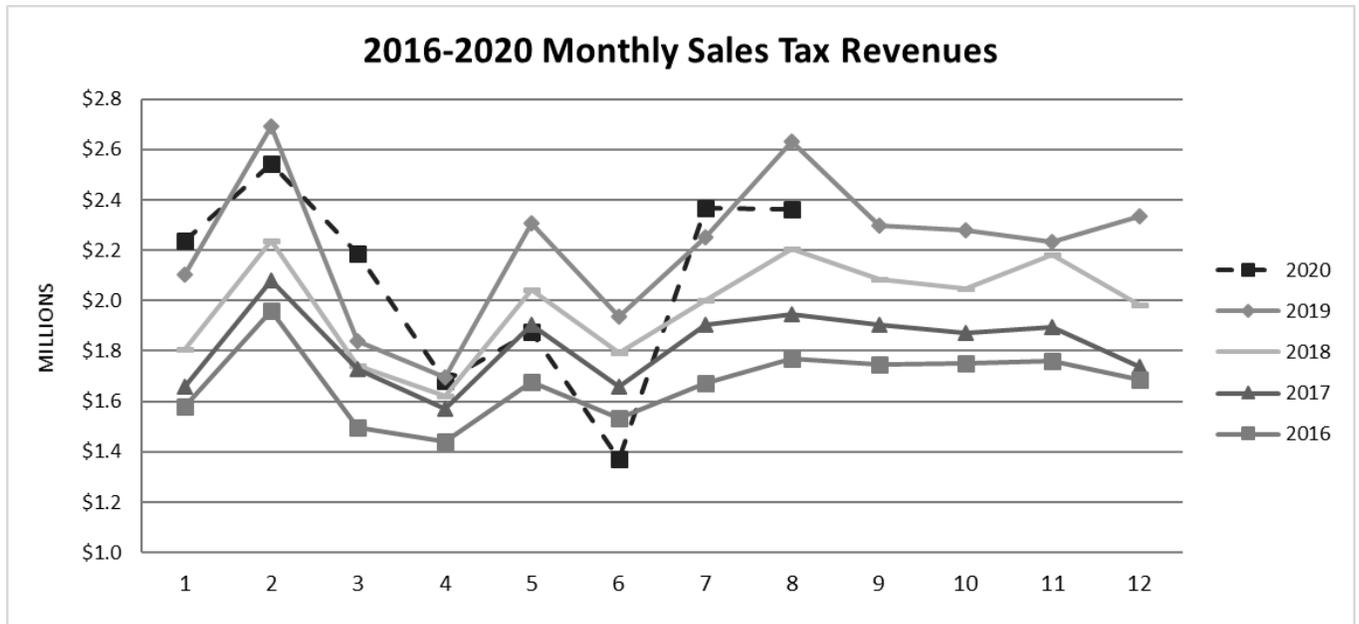
Business Sector Group	YTD		Dollar Change	Percent Change	Percent of Total	
	2019	2020			2019	2020
Services	2,214,049	2,363,028	148,979	6.7%	12.7%	14.2%
Contracting	4,252,234	4,394,861	142,627	3.4%	24.4%	26.4%
Communications	547,177	324,806	(222,371)	-40.6%	3.1%	2.0%
Retail:						
Auto/Gas Retail	3,434,214	2,915,641	(518,574)	-15.1%	19.7%	17.5%
Gen Merch/Misc Retail	1,748,338	1,851,410	103,073	5.9%	10.0%	11.1%
Retail Eating/Drinking	1,211,448	973,602	(237,846)	-19.6%	6.9%	5.9%
Other Retail	2,042,739	2,198,296	155,558	7.6%	11.7%	13.2%
Wholesale	768,769	746,993	(21,776)	-2.8%	4.4%	4.5%
Miscellaneous	1,239,445	867,057	(372,388)	-30.0%	7.1%	5.2%
<b>Total</b>	<b>17,458,413</b>	<b>16,635,695</b>	<b>(822,718)</b>	<b>-4.7%</b>	<b>100%</b>	<b>100%</b>

**Comparing 2020 to 2019, year-to-date (YTD) sales tax revenue is down \$822,718 (4.7 percent).** However, 2019 includes two large back tax payments totaling \$458,733 from the Communications and Miscellaneous business sectors. **Factoring out these one-time payments, YTD sales tax revenue is down 2.1 percent relative to the same period in 2019.**

Looking at business sectors, **the most significant growth occurred in Other Retail (up \$155,558, or 7.6 percent), Services (up \$148,979, or 6.7 percent), Contracting (up \$142,627, or 3.4 percent), and General Merchandise/Miscellaneous Retail (up \$103,073, or 5.9 percent).** The growth in Other Retail has been led by the Electronics and Health & Personal Care sub-sectors. Within Services, the growth has been concentrated in the Administration & Support, Professional Scientific, and Publishing Services sub-sectors.

**Noteworthy declines occurred in Auto/Gas Retail (down \$518,574, or 15.1 percent), Miscellaneous (down \$372,388, or 30.0 percent), Retail Eating/Drinking (down \$237,846, or 19.6 percent), and Communications (down \$222,371, or 40.6 percent).** Most of the drop in Auto/Gas Retail is primarily due to a \$410,305 (83.5 percent) decline in May 2020 (for March retail activity) versus May 2019. The significant decreases in Miscellaneous and Communications respectively relate to back tax payments of \$248,522, which was received in February 2019, and \$210,211, which was received in July 2019. Retail Eating/Drinking is down due to the Governor's stay-at-home order, which was in effect from March 25<sup>th</sup> to May 31<sup>st</sup>, and social distancing requirements, which limit the number of customers that can be served.

The chart below shows Kirkland's monthly sales tax revenue through August 2020 compared to the prior four years.



### “What If” Forecast Scenarios (2020 Only)

Given the high level of economic uncertainty for the balance of the year, three “what if” forecast scenarios are provided in the following table for 2020 sales tax revenue. Note that the 2020 budget of \$23,130,166 reflects the City’s two-year sales tax lag policy (2020 budget = 2018 estimate).

“What If” Scenario	2020 Forecast	2020 Budget	Surplus (Deficit)	Staff Forecast Assessment
2020 forecast is 5% below 2019 actual*	\$25,262,146	\$23,130,166	\$2,131,980	Likely
2020 forecast is 10% below 2019 actual*	\$23,932,560	\$23,130,166	\$802,394	Pessimistic
2020 forecast is 15% below 2019 actual*	\$22,602,973	\$23,130,166	(\$527,193)	Very pessimistic

\*2019 actual sales tax revenue = \$26,591,733.

As previously noted, sales tax revenue for January-August 2020 is down 4.7 percent relative to the same period in 2019. This is considerably better than King County’s August 25, 2020 forecast of annual taxable retail sales, which are projected to decline 14.7 percent in 2020.

**The key “takeaway” from these “what if” forecast scenarios is that 2020 budgeted sales tax revenue is 13 percent below 2019 actual sales tax revenue. That provides a significant “cushion” in 2020, reducing the financial impact of the three scenarios accordingly.**

To help frame staff’s assessment of the three “what if” forecast scenarios, the following three tables identify how much sales tax revenue would have to decline in the last four months of 2020 relative to the last four months of 2019 to end the year 5 percent, 10 percent, and 15 percent below 2019 actual sales tax revenue.

*2020 Forecast is 5% below 2019 Actual (Staff Forecast Assessment: Likely)*

Sales Tax Revenue	2019	2020	\$ Change	% Change
January-August (actual)	\$17,458,413	\$16,635,695	(\$822,718)	-4.7%
September-December (2019 actual & 2020 forecast)	\$9,133,320	\$8,626,451	(\$506,869)	<b>-5.5%</b>
<b>Total</b>	<b>\$26,591,733</b>	<b>\$25,262,146</b>	<b>(\$1,329,587)</b>	<b>-5.0%</b>

*2020 Forecast is 10% below 2019 Actual (Staff Forecast Assessment: Pessimistic)*

Sales Tax Revenue	2019	2020	\$ Change	% Change
January-August (actual)	\$17,458,413	\$16,635,695	(\$822,718)	-4.7%
September-December (2019 actual & 2020 forecast)	\$9,133,320	\$7,296,865	(\$1,836,455)	<b>-20.1%</b>
<b>Total</b>	<b>\$26,591,733</b>	<b>\$23,932,560</b>	<b>(\$2,659,173)</b>	<b>-10.0%</b>

*2020 Forecast is 15% below 2019 Actual (Staff Forecast Assessment: Very Pessimistic)*

Sales Tax Revenue	2019	2020	\$ Change	% Change
January-August (actual)	\$17,458,413	\$16,635,695	(\$822,718)	-4.7%
September-December (2019 actual & 2020 forecast)	\$9,133,320	\$5,967,278	(\$3,166,042)	<b>-34.7%</b>
<b>Total</b>	<b>\$26,591,733</b>	<b>\$22,602,973</b>	<b>(\$3,988,760)</b>	<b>-15.0%</b>

Sales tax revenue would have to decline 5.5 percent, 20.1 percent, and 34.7 percent respectively in September-December 2020 to end the year 5 percent, 10 percent, and 15 percent below 2019 actual sales tax revenue. The latter two reduction scenarios are unlikely provided that a second “stay at home” order is not issued between now and the end of the year.

**For the 2021-2022 Preliminary Budget, staff is conservatively forecasting a 10 percent decline in 2020, which is still \$802,394 greater than the 2020 budget, and no growth in 2021 and 2022, consistent with the City’s modified two-year lag policy.** However, the 2020-2022 sales tax forecast will be subject to change based on the monthly sales tax distributions in September and October as well as other relevant economic data. If necessary, the 2020-2022 sales tax forecast can be adjusted as late as December, when the 2021-2022 Final Budget is adopted by the Council.

### Key Economic Indicators

Information about wider trends in the economy provides a mechanism to help understand current results in Kirkland and to predict future performance. The combination of consumer confidence, unemployment levels, housing data, inflation, and auto sales provides a broader economic context for key factors in sales tax revenues. Since the sales tax figures reported above are from two months prior, some of the figures in the table below can function as leading indicators for where sales taxes may go in future reports.

Indicator	Most Recent Month of Data	Unit	Month			Yearly Average	
			Previous	Current	Change	2019	2020
<b>Consumer Confidence</b>							
Consumer Confidence Index	August	Index	91.7	84.8	(6.9)	128.1	103.5
<b>Unemployment Rate</b>							
National	August	%	10.2	8.4	(1.8)	3.7	8.7
Washington State	June	%	14.8	9.9	(4.9)	4.5	9.1
King County	June	%	14.4	9.6	(4.8)	3.0	8.3
Kirkland	June	%	12.0	7.5	(4.5)	2.9	7.1
<b>Housing</b>							
New House Permits (WA)	June	Thousands	56.6	35.8	(20.8)	48.7	45.1
Case-Shiller Seattle Area Home Prices	June	Index	271.4	272.1	0.6	252.2	265.9
<b>Inflation (CPI-W)</b>							
National	August	% Change	1.0	1.4	0.4	1.7	1.2
Seattle	August	% Change	1.0	2.4	1.4	2.1	1.9
<b>Car Sales</b>							
New Vehicle Registrations	July	Thousands	16.6	21.1	4.5	23.7	17.7

The **Consumer Confidence Index** dropped from 91.7 in July to 84.8 in August. The 2020 average is 24.6 points below the 2019 average.

The national **Unemployment Rate** dropped from 10.2 percent in July to 8.4 percent in August, while the Washington State unemployment rate dropped from 14.8 percent in May to 9.9 percent in June. King County and Kirkland's unemployment rates also fell in June, with the County decreasing significantly from 14.4 to 9.6 percent and Kirkland falling from 12.0 to 7.5 percent.

**New Housing Permits** in Washington State continue to be volatile, falling significantly from 56,600 in May to 35,800 in June. The **Case-Shiller Home Price Index** saw a small increase of 0.6 points in June, and the 2020 average currently sits 13.7 points above the 2019 average, reflecting a strong housing market despite the pandemic.

**Inflation** for Seattle-Tacoma-Bellevue, as measured by the CPI-W, increased from 1.0 percent to 2.4 percent between June and August. On the national level, inflation continued to increase slightly, increasing from 1.0 percent in July to 1.4 percent in August.

**New Vehicle Registrations** increased by 4,500 from June to July, reflecting the third straight month of growth from its low point in April.