FISCAL IMPACTS OF PROPOSED ANNEXATION OF PROPERTIES WEST OF TUMWATER

PREPARED FOR
BEAVER CREEK ACQUISITION COMPANY, LLC

February 2007
INTRODUCTION

This report provides initial results of an annexation analysis project commissioned by Beaver Creek Acquisition Company, LLC (Beaver Creek) to support the City of Tumwater’s evaluation of the potential fiscal impacts of annexing an area to the west of the current City boundary. This potential annexation area (PAA) includes the Doelman Property, which is proposed to be developed by Beaver Creek into a mixed-use urban village. The analysis estimates the potential impacts on City of Tumwater operating revenues and costs, and provides a high-level assessment of the City’s capital program. In addition, the analysis evaluates potential implications of annexation on several entities, with particular attention paid to Fire District 5, which currently provides fire services to the area.

The goal of the analysis is to provide decision makers at the City and key stakeholders including current City residents, residents of the annexation area and other affected jurisdictions with a more complete understanding of the fiscal impacts of annexation, both in terms of the costs the City would bear immediately upon annexation and in the longer term. Berk & Associates worked closely with City staff and Beaver Creek to develop many of the underlying assumptions included in the analysis.

KEY ASSUMPTIONS

The analysis that is summarized in this report is shaped by the following key overarching assumptions:

- The proposed annexation is assumed to take place in June, 2007.

- The proposed annexation area would receive levels of service similar to those now provided to the City of Tumwater.

- The current level of service, staffing and expenditures in Tumwater are the benchmarks for projecting comparable levels of service, staffing and costs in the annexation area. This study does not evaluate whether Tumwater’s existing levels of service, staffing or expenditures are acceptable or sustainable with existing resources and staffing.

- This fiscal analysis includes cost and revenue estimates only for those taxes or services that would change upon annexation. Local services that are assumed to be unaffected by the annexation decision include water and sewer, schools, local transit, and health services.

- While the model is not Fund-based, it does isolate the components of the City’s budget that are funded through general tax and fee revenues, which in the case of Tumwater, includes functions and departments within the General Fund and Asset Management Fund. The model does not include other funds, such as the utility enterprise funds and the golf course fund, since these funds are either not tax-supported or not expected to experience any annexation-related impacts.

- Since the cost of additional Fire department staff related to the staffing of Fire Station 2 will benefit both the annexation area and current City residents the costs assigned to the annexation area are limited to the area’s “fair share” of the entire cost of the department. This area’s fair share will be calculated according to its proportionate share of assessed value (AV).
• The City of Tumwater will enjoy certain economies of scale in delivering City services. In fact, there are several small departments within the City that are assumed to be able to absorb any service impacts associated with the annexation without adding any staff beyond what is already in place.

• This analysis assumes that all initial annexation-related FTEs are hired are in place for the date of annexation. In reality, the City might choose to ramp up its hiring more slowly over time. While the analysis does make estimates of FTE needs at annexation and through the buildout period, actual decisions regarding hiring and staffing will be made by the Council during each budget cycle, based on City priorities and actual demand.

• The only capital costs that are estimated as part of this analysis include the one-time and ongoing equipment costs associated with new staff. These costs include expenses related to information technology for all employees, specialized equipment for Police and Fire department staff, and vehicles for Police department staff.

• Other capital costs, such as those related to public infrastructure like parks and roads, are not considered quantitatively in this analysis. These costs are difficult and expensive to estimate, and any future development in the City will be subject to review as part of the development regulatory process. This process will include public notices, public hearings, and opportunities for the City to require infrastructure-related mitigation fees.

• Current City policies related to capital revenues will continue. These policies include development impact fees, allocations of state gas tax revenues, and allocations of City utility tax revenues to capital funding. The impact fee rates charged today are assumed to hold steady throughout the planning horizon. Therefore, all impact fee estimates are in 2006 dollars. In reality, the City is likely to raise impact fee rates several times between today and 2020. Therefore, estimates of future impact fees are conservative, and could be substantially higher depending on Council direction.

**SUMMARY OF FISCAL IMPACTS ON ANNEXATION**

As Exhibit ES-1 shows, the analysis suggests that annexation yields a net positive fiscal impact on the operations of the City of Tumwater during most of the years in the planning horizon. Costs slightly outpace revenues in 2007, driven mostly by one-time costs associated with annexation and lags in the City’s collection of annexation area revenues. Property tax revenues from the annexation area, for instance, will not accrue to Tumwater until 2009. During the period between the date of annexation and the City’s first receipt of property tax revenues in 2009, the City will receive revenues associated with the County road and fire district levies for the annexation area. Those revenues are currently estimated at approximately $300,000 in 2007 and $500,000 in 2008. These revenues make annexation mostly neutral in 2008, and annexation also appears to be mostly neutral in 2009.

Once development begins on the Doelman Property (currently estimated at 2010), revenues would be significantly enhanced by one-time revenues associated with sales tax and B&O tax on new construction. After the commercial portion of the Doelman Property comes online (currently projected for 2015), the sales tax revenues anticipated from that project are large enough to offset much of the loss in one-time revenues that will take place as the high-development period comes to a close. In terms of net present value (assuming a discount rate of 6%), annexation is estimated to produce a net positive fiscal impact of approximately $2.3 M between 2007 and 2020.
While the overall fiscal impact for the planning period is positive, toward the end of the period the cost and revenue lines begin to converge, and at the end of the period, operating costs are greater than operating revenues. This trend, where municipal service costs are growing at faster rates than revenues, is not surprising and is also likely a phenomenon that will affect the current City even without annexation. This long-term trend is evident in most other cities in Washington and is related to the impact of Initiative 747, which limits growth in property taxes.

Initiative 747 caps the allowed increases in property tax revenue at 1% per year (plus levies on new construction). To exceed 1% municipalities must seek voter approval. With this major revenue source capped at 1% increases per year, and with costs that tend to escalate at levels at least equivalent to inflation (and in cases health care costs and employee benefits, more than inflation), cities across the state are facing the reality of costs that grow faster than their revenues. To address this challenge local governments must either increase their tax base through growth or cut costs to maintain fiscal balance. Regardless of how future Tumwater Councils might choose to address this structural problem, it will generally be easier to manage with the situation as a larger City with a larger tax base in a post-annexation scenario.

### Exhibit ES-1

**Summary of Annexation Area Fiscal Impacts on Operations ($M)**

![Graph showing fiscal impacts](image)

Source: Berk & Associates, City of Tumwater

The capital impacts from annexation are somewhat more difficult to discern. While this analysis does estimate the equipment costs associated with new staff, it only addresses facility and infrastructure costs on a qualitative basis. The analysis does estimate the additional capital revenues available after annexation. The City derives funding for capital facilities from the real estate excise tax; a portion of the gas tax; a portion of the City utility tax (by City policy); and impact fees from development. These revenues are displayed in Exhibit ES-2 below and amount to over $7 M over the planning period in present value terms.
The impact fee portion of capital revenues is likely a conservative estimate. Rates charged today are assumed to hold steady throughout the planning horizon. Therefore, all impact fee estimates are in 2006 dollars. In reality, the City is likely to raise impact fee rates several times between today and 2020. Therefore, estimates of future impact fees could be substantially higher depending on Council direction.

Exhibit ES-2
Estimated Annexation Area Capital Revenues

Source: Berk & Associates, City of Tumwater
CITY OF TUMWATER
FISCAL IMPACTS OF ANNEXATION
Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>INTRODUCTION</td>
<td>1</td>
</tr>
<tr>
<td>ANALYTIC FRAMEWORK</td>
<td>1</td>
</tr>
<tr>
<td>KEY ASSUMPTIONS</td>
<td>3</td>
</tr>
<tr>
<td>STUDY AREA CHARACTERISTICS</td>
<td>5</td>
</tr>
<tr>
<td>OPERATING REVENUE AND COST ANALYSIS</td>
<td>10</td>
</tr>
<tr>
<td>CAPITAL REVENUE AND COST ANALYSIS</td>
<td>17</td>
</tr>
<tr>
<td>IMPLICATIONS OF ANNEXATION ON OTHER ENTITIES</td>
<td>20</td>
</tr>
<tr>
<td>APPENDIX A</td>
<td>23</td>
</tr>
<tr>
<td>APPENDIX B</td>
<td>24</td>
</tr>
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</table>
INTRODUCTION
This report provides initial results of an annexation analysis project commissioned by Beaver Creek Acquisition Company, LLC (Beaver Creek) to support the City of Tumwater’s evaluation of the potential fiscal impacts of annexing an area to the west of the current City boundary. This potential annexation area (PAA) includes the Doelman Property, which is would be developed by Beaver Creek into a mixed-use urban village. The analysis estimates the potential impacts on City of Tumwater operating revenues and costs, and provides a high-level assessment of the City’s capital program. In addition, the analysis evaluates potential implications of annexation on several entities, with particular attention paid to Fire District 5, which currently provides fire services to the area.

The goal of the analysis is to provide decision makers at the City and key stakeholders including current City residents, residents of the annexation area and other affected jurisdictions with a more complete understanding of the fiscal impacts of annexation, both in terms of the costs the City would bear immediately upon annexation and in the longer term. Berk & Associates worked closely with City staff and Beaver Creek to develop many of the underlying assumptions included in the analysis.

ANALYTIC FRAMEWORK
An annexation fiscal model was used for this project to estimate revenues and expenses for the potential annexation area. In this model, factors in the land base (such as population, employment, and commercial activity) drive both demand for services and the tax base. Depending on a jurisdiction’s scope of services and choices regarding level of service, demand for services leads to costs, and depending on a jurisdiction’s choices regarding fiscal and taxing policy (limited by tax laws), its tax base will lead to tax and fee revenues. Exhibit 1 below is a schematic representation of the model.

The analysis assumes annexation in 2007 and examines costs and revenues in the annexation area through 2020, several years after development on the Doelman Property is expected to conclude. Taking the analysis out over time (as opposed to taking a snapshot in time) allows the City to see how the fiscal balance in the annexation area will change over time, both during and after the anticipated periods of development activity.
Exhibit 1
Long-Term Fiscal Model Schematic

LAND BASE
(Current City and Annexation Areas)
Identify vacant and redevelopable land based on parcel-level review of zoning, land use and current values.
Scenarios based on % of maximum buildout, pace of growth, and redevelopment intensity

COMMERCIAL
Square Footage, Type, Scale, Timing, Tenant Mix
Employment
New Retail Activity

RESIDENTIAL
Housing Mix, Type and Density
Housing Units
Population

TAX BASE
Assessed Value
Taxable Retail Sales
Business Income
Utility Usage
Population-based
Employment-based
Development-related
Other

Set Tax and Fee Policies

SERVICE DEMAND
Direct Service Impacts
Estimate direct impacts based on key service drivers (population, employment, land area, other) by department.
Indirect Service Impacts
Estimate indirect impacts based on relationship to direct impacts.

Set Level-of-Service Policy

SERVICE COSTS

NET FISCAL IMPACT
Estimate State Sales Tax Credit

CAPITAL NEEDS

Source: Berk & Associates
Proper Calculation of Future Property Tax Revenues

For the most part, this analysis focuses only on the fiscal performance of Tumwater’s proposed annexation area and does not consider the future fiscal outlook for the current City of Tumwater. Revenues generated from the annexation area are compared to costs associated with incremental staff needed to serve the area. However, due to the nature of the calculation of property tax rates, it is necessary to project assessed values (AV) citywide.

Initiative 747 limits cities in Washington to a maximum property tax levy increase of 1% over the previous year’s levy (plus additional levy revenues from new construction or annexation), unless a larger increase is allowed through a public vote. Because the assessed value of most property increases at a rate greater than 1% per year, the result of I-747 is a lessening over time of the property tax yield of any individual piece of property, and a gradual lowering of the tax (or millage) rate.

If annexed, the annexation area would be taxed at the city’s millage rate, so it is necessary to project how the millage rate might change in the future in order to reasonably predict property tax revenues generated by the area. The future millage rate depends entirely on the future assessed value in the current City, and that assessed value is projected by taking the average rate of construction in the City over the past 11 years and assuming a continuation of that trend through the end of the planning horizon.

Economies of Scale

When thinking about annexation, it is likely that the City of Tumwater will enjoy certain economies of scale in delivering City services. The City will not be required, for example, to hire a second City Administrator, or a second Police or Fire Chief upon annexation. These savings mean that the average cost-per-resident of providing many city services will tend to decrease as the City of Tumwater becomes larger.

Budget Structure

While the model is not Fund-based, it does isolate the components of the City’s budget that are funded through general tax and fee revenues, which in the case of Tumwater, includes functions and departments within the General Fund and Asset Management Fund. The model does not include other funds, such as the utility enterprise funds and the golf course fund, since these funds are either not tax-supported or not expected to experience any annexation-related impacts.

Capital cost implications are specifically included only for the equipment and fleet costs necessary to support the increasing staff levels associated with annexation. Capital cost implications related to facilities and new public infrastructure are excluded from the analysis, but an estimate of the future capital-restricted revenues for the annexation area is provided.

KEY ASSUMPTIONS

The analysis that is summarized in this report is shaped by the following key overarching assumptions:

- The proposed annexation is assumed to take place in summer 2007.
• The proposed annexation area would receive levels of service similar to those now provided to the City of Tumwater.

• The current level of service, staffing and expenditures in Tumwater are the benchmarks for projecting comparable levels of service, staffing and costs in the annexation area. This study does not evaluate whether Tumwater’s existing levels of service, staffing or expenditures are acceptable or sustainable with existing resources and staffing.

• This fiscal analysis includes cost and revenue estimates only for those taxes or services that would change upon annexation. Local services that are assumed to be unaffected by the annexation decision include water and sewer, schools, local transit, and health services.

• While the model is not Fund-based, it does isolate the components of the City’s budget that are funded through general tax and fee revenues, which in the case of Tumwater, includes functions and departments within the General Fund and Asset Management Fund. The model does not include other funds, such as the utility enterprise funds and the golf course fund, since these funds are either not tax-supported or not expected to experience any annexation-related impacts.

• Since the cost of additional Fire department staff related to the staffing of Fire Station 2 will benefit both the annexation area and current City residents the costs assigned to the annexation area are limited to the area’s “fair share” of the entire cost of the department. This area’s fair share will be calculated according to its proportionate share of assessed value.

• The City of Tumwater will enjoy certain economies of scale in delivering City services. In fact, there are several small departments within the City that are assumed to be able to absorb any service impacts associated with the annexation without adding any staff beyond what is already in place.

• This analysis assumes that all initial annexation-related FTEs are hired are in place for the date of annexation. In reality, the City might choose to ramp up its hiring more slowly over time. While the analysis does make estimates of FTE needs at annexation and through the buildout period, actual decisions regarding hiring and staffing will be made by the Council during each budget cycle, based on City priorities and actual demand.

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STUDY AREA CHARACTERISTICS

The map in Exhibit 2 shows the relationship between the proposed annexation and the current City of Tumwater boundary. The map in Exhibit 3 zooms in on the proposed annexation area and makes special note of the Doelman Property. Beaver Creek Development, who commissioned this project, has entered into a purchase and sale agreement for the Doelman Property.
Exhibit 2
City of Tumwater and Potential Annexation Area

Source: City of Tumwater, Berk & Associates
Exhibit 3
Potential Annexation Area

Source: Berk & Associates, City of Tumwater
Current Conditions in the Annexation Area

Estimates of current population, housing units, and assessed value in the annexation area are based on GIS analysis of Thurston County Assessor’s data extracts and Thurston County parcel shapefiles. Current retail sales tax estimates in the annexation area are based on Berk & Associates’ analysis of the Washington State Department of Revenue’s spatial analysis of taxpayers in the area. In addition to taxable sales generated on-site by businesses, Berk & Associates also estimated sales taxes on the construction activity anticipated in the area.

The annexation area currently contains approximately 850 dwelling units (predominantly single-family), comprising a population of approximately 2,300. The total assessed value in the area is approximately $200 million, and the area currently produces approximately $1 million in taxable retail sales.

Development and Growth

Within the annexation area, growth is expected to come from three primary sources:

- The Doelman Property;
- Parcels with other development already planned or permitted by Thurston County; and
- Vacant or redevelopable parcels

Redevelopable parcels are identified according to the ratio of land value to improvement value. In the parcels identified as vacant or redevelopable, land is set aside for wetlands and other critical area, as well as roads, right-of-ways, churches, schools, and parks. The results of this development potential are shown in Exhibit 4, in terms of single- and multi-family housing units, and the population that those housing units will likely generate.
In total, the annexation area is projected to accommodate approximately 1,850 new housing units which will lead to an additional population of 4,400 for a “buildout” population of 6,700. Since the majority of this growth is estimated to be on either the Doelman property or is otherwise already permitted, the analysis assumes that all of this activity will occur by 2020.

In terms of commercial development, there is an estimate of 150,000 sq ft of commercial development as part of the Doelman property, allocated two-thirds to retail and one-third to office uses. There are also three vacant parcels in the annexation area currently zoned as Light Industrial, which are projected to develop into a possible 200,000 sq ft of light industrial activity. Given the relatively small amount of commercial activity outside of the Doelman property, it is assumed that all of the commercial development will occur by 2020.

While estimates for buildout of the Doelman Property come from Beaver Creek, it is worth noting that the plan for this property is currently at a purely conceptual stage. There will likely be substantial changes to the plan for buildout before the eventual development plan reaches any permitting process.

Property Values

In future years, this base value is expected to revalue at a rate 1% above inflation. Additional assessed value will also be added to the area through development. For the Doelman Property, projections are based on conceptual estimates from Beaver Creek. For other parts of the annexation area, current assessed value per-unit rates are utilized.

Exhibit 4
Residential Development in Potential Annexation Area

<table>
<thead>
<tr>
<th>Single-Family Housing Units</th>
<th>2006</th>
<th>Incr. Adds</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Doelman Property</td>
<td>850</td>
<td>850</td>
<td></td>
</tr>
<tr>
<td>Other Permitted Development</td>
<td>400</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Vacant and Redevelopable Parcels</td>
<td>200</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Annexation Area</td>
<td>800</td>
<td>1,450</td>
<td>2,250</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Multi-Family Housing Units</th>
<th>2006</th>
<th>Incr. Adds</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Doelman Property</td>
<td>250</td>
<td>250</td>
<td></td>
</tr>
<tr>
<td>Other Permitted Development</td>
<td>0</td>
<td>0</td>
<td></td>
</tr>
<tr>
<td>Vacant and Redevelopable Parcels</td>
<td>150</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Annexation Area</td>
<td>50</td>
<td>400</td>
<td>450</td>
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</tbody>
</table>

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<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Doelman Property</td>
<td>2,600</td>
<td>2,600</td>
<td></td>
</tr>
<tr>
<td>Other Permitted Development</td>
<td>950</td>
<td>950</td>
<td></td>
</tr>
<tr>
<td>Vacant and Redevelopable Parcels</td>
<td>850</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Annexation Area</td>
<td>2,300</td>
<td>4,400</td>
<td>6,700</td>
</tr>
</tbody>
</table>

Source: Berk & Associates, City of Tumwater, Beaver Creek
Retail Sales

One of the key revenue sources that cities rely on is retail sales tax. While there is little retail activity currently in the annexation area, the urban village projected for development on the Doelman Property will include substantial additions to the taxable retail sales base. This retail portion of this urban village is estimated to generate approximately $200 of taxable retail sales per square foot, and the office portion approximately $25 per square foot. The other light industrial development is also estimated to generate sales of approximately $25 per square foot. The $200 per foot estimate is based on an overall average for “typical” retail activity. Actual sales tax impacts could be higher or lower depending on the actual types of tenants that might locate in this center.

OPERATING REVENUE AND COST ANALYSIS

In Tumwater, as in most cities, the majority of the City’s costs are concentrated in a relatively small number of service categories, and the majority of revenues accrue from a small number of sources. This section provides a brief overview of these central revenue and cost categories. More detailed estimates of revenues and expenditures are included in Appendix A of this document.

Major Revenues

Upon annexation, five major sources of revenues would flow to the City. These revenues are shown in Exhibit 5, and described in further detail below. Also noted in Exhibit 5 is the portion of revenues in each year that flow from development on the Doelman Property. The property is expected to produce nearly half the annexation area’s total revenues after the commercial portion of the property comes on-line (currently estimated around 2015).

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2012</th>
<th>2016</th>
<th>2020</th>
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</thead>
<tbody>
<tr>
<td>Sales Tax</td>
<td>400</td>
<td>700</td>
<td>1,150</td>
<td>600</td>
</tr>
<tr>
<td>Property Tax</td>
<td>0</td>
<td>900</td>
<td>1,500</td>
<td>1,700</td>
</tr>
<tr>
<td>Utility Tax</td>
<td>100</td>
<td>150</td>
<td>250</td>
<td>300</td>
</tr>
<tr>
<td>B&amp;O Tax</td>
<td>100</td>
<td>150</td>
<td>300</td>
<td>200</td>
</tr>
<tr>
<td>Building and Planning Permits and Fees</td>
<td>250</td>
<td>400</td>
<td>450</td>
<td>700</td>
</tr>
<tr>
<td>Other Taxes and Fees</td>
<td>700</td>
<td>350</td>
<td>600</td>
<td>700</td>
</tr>
<tr>
<td>Total</td>
<td>1,550</td>
<td>2,650</td>
<td>4,250</td>
<td>4,200</td>
</tr>
<tr>
<td>Total from Doelman Property</td>
<td>0</td>
<td>850</td>
<td>2,150</td>
<td>1,850</td>
</tr>
<tr>
<td>% from Doelman Property</td>
<td>0%</td>
<td>32%</td>
<td>51%</td>
<td>44%</td>
</tr>
</tbody>
</table>

Source: Berk & Associates, City of Tumwater

Property Tax

As noted above, the annexation area would be taxed at the city’s millage rate, so it is necessary to project the future of that rate out over time in order to reasonably estimate property tax revenues generated by the area. The assumed City general property tax rate is shown in Exhibit 6 below, along with historical rates since the implementation of I-747’s levy limits. The future millage rate depends entirely on the future assessed value in the current City.
Because of the method for calculating a city’s property tax levy (1% of the previous year’s levy plus new construction), the amount of new construction in a city is important to a city’s ability to avoid erosion of its millage rate. A typical measure of the level of new construction activity in a city is the percent of a city’s total assessed value that comes from new construction in a given year. Projections of this measure are shown in Exhibit 7 below. For the current City of Tumwater (solid blue dots), projections are calculated by determining the average rate of construction in the City over the past 11 years (approximately 2.6% of total assessed value) and assuming a continuation of that rate through the end of the planning horizon. For the annexation area (white dots with blue outline), construction rates are based on conceptual estimates from Beaver Creek, as well as Berk & Associates estimates for other parcels that are vacant, redevelopable, or already planned or permitted by Thurston County. Because the current City has a much larger assessed value base than the annexation area, the impact of new construction on the overall construction rate of the City (black line) is minimal, and the construction rate of the overall City (including the annexation area) tends to trend closely to the construction rate for the current City.

Due to lags associated with annexation and levying, the City will not begin to receive property tax revenues from the annexation area until 2009. Between annexation and 2009, however, the City will receive revenues associated with the County road and fire district levies. Assuming annexation is completed in the summer of 2007, the City would receive approximately half of these levies in 2007, and the full amount in 2008. These revenues are currently estimated at approximately $300,000 in 2007 and $500,000 in 2008. Starting in 2009, the City will receive property tax revenues from the annexation area, and at that point, the City will no longer receive any revenues from the County road and fire district levies. The road levy revenues must be allocated to transportation-related capital expenses. To offset these capital revenues, the City would have flexibility to adjust the portion of utility tax revenues currently allocated to capital back to the General Fund during 2007 and 2008.
Sales Tax

Of the 8.4% sales tax currently collected in the City and the potential annexation area, a 1% “local” share of the tax accrues to local jurisdictions. In the unincorporated area, the full 1% local tax accrues today to Thurston County (with the exception a small portion that is retained by the State Department of Revenue to cover collection and distribution costs). If the transaction location is within a city like Tumwater, the city receives 85% of the 1% local tax and the County receives 15%. This tax is levied not only on businesses in the area, but also on construction activity and some transactions that are related to housing, such as certain online purchases.

B&O Tax

This tax applies to the gross revenues of most businesses at a rate of one-tenth of one percent (0.10%). Like sales tax, this tax is levied not only on businesses in the area, but also on construction activity.

Utility Tax

The City of Tumwater imposes utility taxes on telephones (land-line and cellular), electricity, natural gas, solid waste, water, sewer, and storm drainage, all at a rate of 6%. Current council policy direction allocates half of utility tax revenues to the General Fund, with the remainder transferred to the Capital Improvement Fund to help implement elements of the City’s Capital Facilities Plan.

Building and Planning Permits and Fees

Because of the substantial levels of development projected in the annexation area, fees associated with construction will play a fairly large role in the overall revenue flowing into the City of Tumwater.
should annexation occur. However, it is important to note that these revenues tend to have corresponding costs in the Development Services department for staff time devoted to permit review and plan check responsibilities. The cost recovery rate of this department will be discussed in further detail below.

**Major Costs**

**Staffing Levels**

The estimate of the impact on City service costs begin with an analysis of the need for additional staffing related to changes in demand resulting from annexation and projected buildout in the area. These FTE impact estimates were made through a combination of discussions with City staff (mostly at the Department Director level) and additional analysis regarding levels of service and FTEs per capita. Exhibit 8 below shows FTEs by department in 2006 (current), 2007 (annexation year), and 2020 (end of buildout), as well as the incremental additional FTEs needed for annexation and the resulting buildout. The analysis includes a very conservative assumption that all of the initial annexation-related positions would be in place by the date of annexation (assumed to be summer 2007).

**Exhibit 8**
Core FTEs by Department

<table>
<thead>
<tr>
<th>Department</th>
<th>2006</th>
<th>Annex.</th>
<th>2007</th>
<th>Buildout</th>
<th>2020</th>
</tr>
</thead>
<tbody>
<tr>
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*Parks & Recreation Department FTEs do not include employees related to the municipal golf course.

**Public Works FTEs represent an allocation that removes a portion of FTEs related to Utility Enterprise Funds.**

Source: Berk & Associates, City of Tumwater

The annexation and buildout impacts of each City department are described in further detail below:

**Administration, Finance, General Services, Legal.** These are small departments with the capacity to absorb significant population growth without the need for additional FTEs.

**Development Services.** This department is closely related to development and construction. The City estimates the need for an additional three FTEs at annexation; another two FTEs are assumed to be needed by the end of buildout. This department is supported in part by permit fees related to inspection, planning, and engineering. It is assumed that approximately 70% of the incremental costs associated with new FTEs in this department are recovered through these fees. Thus, only 30% of these costs need to be recovered through general tax revenues generated in the annexation area.
This 70% figure reflects historical cost recovery rates seen in the entire department. Because the cost recovery rate covers the entire department (including the Director and other supervisors), it is likely that the true cost recovery rate of each incremental position added to the department will be higher. Therefore, using 70% as a cost recovery rate represents a fairly conservative estimate. The cost recovery rate will also depend on what portion the City will assume of the costs associated with reviewing development already permitted by Thurston County. This should be one of the topics discussed as part of City-County annexation negotiations.

**Fire Protection Services.** The department estimates a need for ten additional FTEs to staff Station 2 full-time (currently this station is unstaffed), with four positions starting at annexation, and the rest added over time. These additional FTEs are needed not only to serve the annexation area, but the current City as well. Since the cost of additional Fire department staff related to the staffing of Fire Station 2 will benefit both the annexation area and current City residents the costs assigned to the annexation area are limited to the area’s “fair share” of the entire cost of the Fire Department. This area’s fair share is calculated according to its proportionate share of assessed value.

Annexation would have fire-related implications not only for the staffing of the Tumwater Fire Department, but also for the special purpose Thurston County Fire District 5, which currently provides fire services to the area. These implications are discussed in greater detail in Appendix B.

**Parks & Recreation.** At a conceptual level, the City might want a new community park in the annexation area, but no park plan has been developed for the area, nor has a potential site been identified. However, to be conservative, one recreation-related FTE is estimated to be needed by the end of buildout to serve this potential new community park in the annexation area.

**Planning & Facilities.** All additional FTEs in this department are Groundskeepers. At annexation, one FTE is required; another FTE is assumed to needed before the end of buildout, again related to a potential new community park in the annexation area. There is also the potential that a third FTE will be needed to take care of a trail (currently an abandoned railroad) that might eventually become part of the City. This third FTE is not included in this analysis.

**Police.** Three additional patrol FTEs are estimated to be needed at annexation, with an additional three added before the end of planning period. Besides the additions to patrol FTEs, one supervisory FTE is assumed to maintain current span-of-control levels. Patrol estimates from the department were confirmed using the Berk & Associates Police Demand Model.

Given the challenges that cities have faced when trying to forecast police demand in unincorporated areas using traditional techniques, Berk & Associates has developed a robust model for estimating police demand based on the fundamental characteristics of a given area and built on statistical analyses of the experiences of 170 cities across Washington State. Berk & Associates analyzed the relationship between police staffing in cities across the state with the fundamental characteristics of those cities. Through multi-factor regression analyses, strong statistical relationships were identified between police staffing and each city’s unique mix of housing types and tenure, level of commercial activity, geographic area to be policed, and the relationship between a city and nearby major highways and arterials.
Overall, when applied to 170 cities across the state, the Police Demand Model “explains” 96% of the variation in police staffing among cities (in statistical terms, the variation in costs are what one would expect to see given each city’s unique mix of fundamental characteristics).

**Public Works.** One FTE is estimated to be needed at annexation, related to street maintenance in the annexation area; another FTE is assumed to be needed by the end of buildout, given that the area’s roads will be used more intensely as density increases.

**Economies of Scale**

Exhibit 9 shows rates of change of population and FTEs in the annexation area. For the purposes of this analysis, no development is assumed to take place in the current City of Tumwater. Therefore, the impact of annexation and buildout on FTEs per 1000 population can be examined.

The Fire Department is excluded from this analysis because, as noted above, the Fire Department has staffing needs regardless of the question of annexation, and any staffing additions would serve both the annexation area and parts of the existing city.

### Exhibit 9

**Economies of Scale: Population and Core FTEs**

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<th>Population</th>
<th>Core FTEs (Exc. Fire)</th>
<th>FTEs/1000</th>
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<td>13,100</td>
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<td><strong>% Change</strong></td>
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<td>16.5%</td>
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Source: Berk & Associates, City of Tumwater

The table shows that FTE growth does not keep up with population growth, and that the City’s core FTEs (excluding Fire) per 1000 population will drop from 7.89 in 2006 to 7.23 at annexation and 6.08 at buildout. Staffing per capita tends to decrease as cities increase in size. This decrease occurs because larger cities can achieve greater economies of scale in providing service. For instance, there are many positions within the City of Tumwater (department directors, for example) that are fixed, and will not increase with population growth. In addition to department-level economies of scale, the following departments are assumed to be unaffected by the proposed annexation:

- Administration
- Finance
- General Services (Human Resources)
- Legal
Estimating Total Service Cost Impacts

FTEs are translated into labor and non-labor costs using current cost-per-FTE levels particular to each department. Average department salaries tend to be higher than incremental salaries, due to the higher salaries typically paid to department directors and other supervisors. Therefore, using current average salaries has the potential to somewhat overestimate labor costs, making it a conservative estimate. Another conservative assumption used in the analysis is the anticipated rate of escalation of staff salaries, which are projected to increase at a rate of 5% per year. Benefits are projected to increase at a rate of 6% per year.

Summary of Findings

As Exhibit 10 shows, the analysis suggests that annexation yields a net positive fiscal impact on the operations of the City of Tumwater during most of the years in the planning horizon. As noted above, during the period between annexation (assumed to be summer 2007) and the City's first receipt of property tax revenues in 2009, the City will receive revenues associated with the County road and fire district levies. Those revenues are currently estimated at approximately $300,000 in 2007 and $500,000 in 2008. These revenues make annexation mostly neutral in 2008, and annexation also appears to be mostly neutral in 2009.

Once development begins on the Doelman Property (currently estimated at 2010), revenues would be significantly enhanced by one-time revenues associated with sales tax and B&O tax on new construction. After the commercial portion of the Doelman Property comes online (currently projected for 2015), the sales tax revenues anticipated from that project are large enough to offset much of the loss in one-time revenues that will take place as the high-development period comes to a close. In terms of net present value (assuming a discount rate of 6%), annexation has a net positive impact of approximately $2.3 M.
After the addition of the commercial activity from the Doelman Property, the cost and revenue lines begin to converge, and in the outer years, operating costs are greater than operating revenues. This trend, where municipal costs grow at faster rates than revenues, is likely to occur not only in the annexation area, but also in the current City of Tumwater and many other cities in Washington as well. Initiative 747 caps the allowed increases in property tax revenue at 1% per year (plus levies on new construction). With this major revenue source capped at 1% increases per year, and with costs that tend to escalate at levels at least equivalent to inflation (and in cases like salaries and benefits, more than inflation), cities across the state are facing the reality of costs that grow faster than their revenues. Whatever solution Tumwater enacts to deal with this structural problem will be made easier with the larger tax base that would be in place in a post-annexation City.

**CAPITAL REVENUE AND COST ANALYSIS**

This section provides a brief overview of capital costs and revenues for the annexation area. Costs associated with capital include equipment, facilities, and infrastructure. The only capital costs that are estimated as part of this analysis include the one-time and ongoing equipment costs associated with new staff. These costs include expenses related to information technology for all employees, specialized equipment for Police and Fire department staff, and vehicles for Police department staff.

Other capital costs, such as those related to public infrastructure like parks and roads, are not considered quantitatively in this analysis, in part because these costs are difficult and expensive to estimate. Furthermore, any future development in the City (including development in the annexation area) will be subject to review as part of the development regulatory process. This process will include
public notices, public hearings, and opportunities for the City to require infrastructure-related mitigation fees.

As capital costs are fully fleshed out, there may be more needs than there are resources coming from the annexation area. This situation would not be entirely different from the current City, which has unfunded portions of its current capital needs. However, it may turn out that the annexation area produces more capital revenues than it has needs. In that case, those additional revenues would be applied to capital needs in the rest of the City.

**Capital Costs**

**Equipment Costs**

Equipment costs related to new FTEs include a car and equipment for Police FTEs ($50,000 per FTE), equipment for Fire FTEs ($8,762 per FTE), and general equipment (mostly technology-related) for other FTEs ($1,945 per FTE).

**Facilities Costs**

City Hall and Police facilities are already utilized at levels close to capacity. The facilities department estimates that City Hall could only hold 2-3 more FTEs before an expansion would be necessary. Depending on how the City chooses to address its overall facilities needs, the annexation area would cover some share of those costs through taxes. As noted above, the Fire Department has a vacant station in Fire Station 2, so facilities needs are not pressing for this department.

**Infrastructure Costs**

While the information on infrastructure needs and costs in the annexation area is somewhat sparse, there will certainly be substantial costs associated with improving roads from Thurston County standards to Tumwater standards. Some of these costs could potentially be assumed by the County; this is one of the topics that should be discussed as part of annexation negotiations between the City and the County. Upon annexation, the City would need to prioritize the necessary improvements into high and low priority items and work out the plan to meet these goals. Some of the improvements may need to see a more immediate action; however, it is reasonable to presume that most of the capital improvements will be done over time, potentially even over the next several decades.

**Capital Revenues**

While capital-related costs associated with the annexation area are difficult to estimate, additional capital-related revenues can be estimated with some confidence. These capital-related revenues come from the real estate excise tax; a portion of the gas tax; a portion of the City utility tax; and impact fees from development can be estimated with some confidence. These revenues, which total over $11 M between 2007 and 2020 (or more than $7 M in present value), are displayed in Exhibit 11, and described in further detail below.
Real Estate Excise Tax (REET)

By statute, cities must use REET revenues to fund capital investments. REET revenues are levied in two halves: The first half (0.25% of the taxable value of a real estate transaction) may be used for a variety of capital uses, including development of parks. The second half (the second 0.25%) must be used on a more constrained list of projects; a list that includes improvements to roads and roadways, but excludes investments in parks.

The amount of REET revenues a city receives tends to vary substantially from year to year. During years when the real estate market is active, revenues are high, and during softer real estate markets, revenues are low. For the purposes of this analysis, it is assumed that 5% of residential property and 2% of commercial property turn over in any given year. These turnover rates are likely low compared to long-term rates in the area. However, given that much of the activity in the area will be comprised of new sales, and given the uncertainty around turnover rates for these new properties, using relatively low turnover rates represents a conservative estimate.

Motor Vehicle Fuel Excise Tax (Gas Tax)

Until 2005, cities had been receiving their gas tax in two distributions: a restricted portion (32%) to be used for capital; and an unrestricted portion (68%) allowed to be used for operating or capital funding. Recently, however, the dual-distribution and restriction have been removed, but most cities (including Tumwater) have continued to allot 32% of gas tax revenues to their capital program. It is assumed going forward that Council direction on this issue will not change.

Utility Tax

As noted above, Tumwater allocates half of utility tax revenues to the Capital Improvement Fund to help implement elements of the City’s Capital Facilities Plan. It is assumed that this policy direction will...
continue, such that half of any utility tax revenue generated by the annexation area is set aside as capital revenues.

**Development Impact Fees**

Tumwater has development impact fees related to transportation, parks, and fire protection. Transportation impact fees are charged according to the number of residential dwelling units developed and the square feet of commercial space developed; parks impact fees are charged according to the number of residential dwelling units developed; and fire protection impact fees are charged according to the square feet of residential and commercial space developed. The impact fee rates charged today are assumed to hold steady throughout the planning horizon. Therefore, all figures in Exhibit 12 are in 2006 dollars. In reality, the City is likely to raise impact fee rates several times between today and 2020. Therefore, estimates of future impact fees are conservative, and could be substantially higher depending on Council direction. Detail of projected revenues from the three impact fees is displayed in Exhibit 12 below.

### Exhibit 12

**Estimated Development Impact Fee Revenues**

![Graph showing estimated development impact fee revenues](source: Berk & Associates, City of Tumwater)

**IMPLICATIONS OF ANNEXATION ON OTHER ENTITIES**

The purpose of this analysis is to estimate the fiscal impact of annexation on the City of Tumwater. However, there are implications from annexation for other entities besides the City.

**Fire District 5**

The implications of annexation for special purpose Thurston County Fire District 5 are likely to be significant, as annexation would result in the following:

- A reduction of approximately 30% of the District’s assessed value;
- The likely dissolution of Fire Station 52, near the northeastern shore of Black Lake;
- A remaining “peninsula” of land to the east of Black Lake that would be difficult to serve out of Fire Station 51 (Exhibit 13 below displays this geographic challenge);
Exhibit 13
Fire District Boundaries and Proposed Tumwater Annexation

Source: Thurston County, City of Tumwater, Berk & Associates
• Difficulty maintaining current levels of staffing with a reduced property tax base;

• State law can require a transfer of assets among districts in the case of a change in governance. In this case, it is estimated that the District would be required to transfer approximately 30% of the current value of its assets, valued at approximately $1.4 M. In practice, asset transfer agreements are subject to negotiation and rely on communication between the affected parties.

All told, the District would be left with an economic base and geographic layout that would make it difficult to provide adequate levels of service to its remaining service area. A more complete discussion of the implications for Fire District 5 is included in Appendix B.

**Thurston County**

Thurston County would lose both the costs and revenues associated with serving the annexation area. Furthermore, there are several issues related to potential reimbursement that ought to be negotiated between the County and the City of Tumwater. These issues include the review of development already permitted by the County, as well as the condition of county roads in the annexation area.

**Residents of the Current City of Tumwater**

There are several tax implications for current residents of Tumwater. If annexation occurs, it will change the assessed value of the city. For the current bond levy (and potential future bonds), then, residents of the annexation area would pay their fair share according to assessed value, which would lessen the amount required of current city residents. If the annexation area had been part of the City in 2006, for example, residents of the current City would have realized savings of approximately $110,000, as their debt burden would have decreased from $820,000 to $710,000.

There is also a level of service implication related to the Tumwater Fire Department. Because annexation will likely cause the Fire Department to staff Station 2 at least part time, annexation will increase the level of service across the entire City.

**Residents of the Annexation Area**

Residents of the annexation area would realize tax and level of service implications as well. Based on 2006 rates, their overall property taxes would be slightly lower. While they would no longer pay the County road levy, they would begin paying a fair share of debt related to existing general obligation bonds for the City of Tumwater. Besides those Tumwater bonds, residents of the annexation area would continue to pay their share of bonds associated with Fire District 5 (only those bonds related to debt; not to current service). Residents would also begin to pay the utility taxes levied by the City.

Residents’ levels of service would likely increase, especially with regards to public safety, as they moved from rural to urban providers of service. A similar increase would likely occur with fire service, as residents moved from fire service rated 8A by the Insurance Services Office (ISO) to service rated 5. ISO’s scale goes from 1 to 10, where 1 represents exemplary public protection and 10 indicates that the area’s fire-suppression program doesn’t meet ISO’s minimum criteria. ISO is a data supplier for the insurance industry, and their Public Protection Classification Program rates fire service providers on a number of different axes, including equipment, staffing, training, and water supply.
### Annexation Costs ($'000)

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<td>360</td>
<td>380</td>
<td>400</td>
<td>420</td>
<td>440</td>
<td>460</td>
<td>600</td>
<td>630</td>
<td>660</td>
<td>700</td>
</tr>
<tr>
<td>Other Taxes and Fees</td>
<td>470</td>
<td>930</td>
<td>480</td>
<td>540</td>
<td>680</td>
<td>750</td>
<td>810</td>
<td>890</td>
<td>970</td>
<td>1,040</td>
<td>1,220</td>
<td>1,280</td>
<td>1,330</td>
<td>1,410</td>
</tr>
<tr>
<td>Total</td>
<td>790</td>
<td>1,470</td>
<td>1,640</td>
<td>2,190</td>
<td>2,360</td>
<td>2,630</td>
<td>3,150</td>
<td>3,720</td>
<td>3,910</td>
<td>4,210</td>
<td>3,760</td>
<td>3,900</td>
<td>4,050</td>
<td>4,210</td>
</tr>
</tbody>
</table>

### Surplus/Deficit ($'000)

|                      | (70) | 50  | (50) | 470 | 410 | 380 | 840 | 790 | 820 | 700 | (30) | (70) | (430) | (420) |

Source: Berk & Associates, City of Tumwater
APPENDIX B
ASSESSMENT OF FINANCIAL AND CAPITAL IMPLICATIONS FOR FD 5

PURPOSE

The information below analyzes the potential effects of annexation on fire protection and emergency medical services within Fire District (FD) 5. Specifically, the following section examines the capital costs, governance, and the legal and practical implications of transferring assets across districts.

It should be noted that a small portion of FD 11 is included in the southernmost region of the Proposed Annexation Area (PAA). However, the resulting annexation should have little to no impact on fire and emergency services within the service area of the District, as the annexation would result in the loss of only 0.7% of FD 11’s total area. As such, this appendix focuses on the issues raised for FD 5, which would experience a far greater impact as a result of the annexation.

Through interviews with FD 5’s Black Lake Fire Department (BLFD) Chief and Operating Manager, Berk & Associates has identified cost and revenue estimates for fire services under different scenarios. While the City of Tumwater has expressed its intention to provide fire services to the PAA by its own fire department after annexation, several alternatives exist for FD 5 in supplying services to the remainder of constituents living within District boundaries. These alternatives will be presented and discussed as possible approaches for maintaining the current level of fire service provided by FD 5.

SUMMARY OF FINDINGS

As a result of the annexation, the BLFD will likely be unable to maintain its current staffing levels and operational facilities in FD 5, due to a thirty percent reduction in property tax revenue for operations. The closure of at least one of its two fire stations appears to be a probable outcome, as BLFD will neither have the funds nor the manpower to continue manning both stations. These impacts come on the heels of the rejection by voters in 2006 to raise the operating levy rate to fund current operations by hiring two more career firefighters. Currently, the District has five career firefighter positions, though a significant share of the cost of three of these positions is being covered by a one-time grant of $310,500 by the U.S. Department of Homeland Security. By 2011, 100% of the cost of these personnel costs will be borne by the District. The District’s goal is to maintain a minimum staffing of at least one career firefighter on duty at all times for emergency response.

FD 5 has a few practical options to choose from after a successful annexation. In one scenario, FD 5 can partially or fully merge with neighboring fire districts 9 or 11. In another scenario, the BLFD can be completely dissolved and enter into a contractual agreement with the City of Tumwater to provide service to all residents living in FD 5. Or, if the BLFD chooses to remain active and retain its own fire district, it will likely need to enter an agreement with Tumwater to provide partial service to residents living in FD 5, as the annexation area would leave a small portion of service area to the east of Black Lake that would be difficult to serve effectively or efficiently. Regardless, an increase in fire-response response time will be a likely outcome for those living northeast of Black Lake due to its geographic isolation after annexation relative to the rest of FD 5.
BACKGROUND

FD 5 – Challenges

Fire District 5, operating as the Black Lake Fire Department (BLFD) provides fire protection services for an area of approximately 12 square miles located along the City of Tumwater’s northwestern border. BLFD, which provides fire and emergency services to the District’s roughly 9,000 inhabitants, operates two fire stations (Station 51 and Station 52). The Department currently staffs five paid career firefighters (including the fire chief) and roughly 40 volunteer firefighters working for the Department. At a minimum, BLFD maintains one paid firefighter and two resident volunteer firefighters (who live at the station) on active duty. Under their current budget constraints, having resident volunteers allows FD 5 a way to creatively compensate staff (through room and board) without incurring many real costs. The recent hiring of three paid, full-time firefighters has made it possible to staff both stations at all times.

The proposed annexation would create several operational, financial, and logistical challenges for FD 5. Sixty percent of FD 5’s fire service-related calls come from the PAA, in part due to its high population density relative to the rest of the District (the PAA accounts for only 28% of assessed value in FD 5). Additionally, 30% of FD 5’s assessed value is derived from the PAA, which would translate into a revenue loss of $297,406 for 2007 (Exhibit B-1). As the property tax levy represents 96 percent of the District’s funding, this would signify a major reduction in operating revenue.

<table>
<thead>
<tr>
<th>Implications of Annexation for FD 5 Property Tax Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fire District 5</td>
</tr>
<tr>
<td>------------------</td>
</tr>
<tr>
<td>$693,099,165</td>
</tr>
<tr>
<td>Annex Area within FD 5</td>
</tr>
<tr>
<td>FD 5 Revenue After Annexation</td>
</tr>
</tbody>
</table>

Source: Berk & Associates, Black Lake Fire Department

Fire Stations. Such a precipitous drop in fire service calls and revenue raises questions about the necessity and viability of two operational fire stations within FD 5 once Tumwater begins providing its own fire service to the PAA after annexation. Most likely, Fire Station 52, located along Black Lake’s northeastern border, will be dissolved due to its proximity to the PAA and its geographic constraints to the rest of the District. Fire Station 51, which was recently built at a cost of $2.5 million, has the potential to remain operational, depending upon BLFD’s ability to continue effectively providing fire coverage to the remaining residents living within the district with such financial and operational limitations.

Staffing. In 2006 FD 5 was awarded a one-time grant of $310,500 by the U.S. Department of Homeland Security, an endowment dedicated to the recent hiring of three full-time firefighters. In the first year (2007), the grant covers 90 percent of the new employees’ wages, and will continue to provide funding at a decreasing rate over the following three years (Exhibit B-2). By the fifth year, FD 5 is obligated to pay 100 percent of the three firefighters’ salaries. Due to the acceptance of this grant, FD 5 is financially committed to the grant for five years, as the firing or laying-off of personnel (without replacement) would entail paying back the grant in its entirety. In reviewing FD 5’s operating budget
and estimated revenue streams over the next five year, it is appears that the BLFD will not be able to sustain its current level of five firefighters after annexation (Exhibit B-2). As a result, BLFD might not possess the capacity to effectively operate even one fire station.

### Exhibit B-2

**Employment Implications of Proposed Annexation**

<table>
<thead>
<tr>
<th>Year</th>
<th>Cost of 3 New Firefighters (approx. $50,000 per year)</th>
<th>Grant Covering 3 New Firefighter Positions</th>
<th>Share FD 5 Pays for 3 New Firefighter Positions</th>
<th>FD 5 Projected Budget With 3 New Firefighters</th>
<th>Revenue (after annexation) - Estimated 3% Growth</th>
<th>FD 5 Budget Shortfall (Revenue - Budget)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>$150,000</td>
<td>$100,486</td>
<td>$49,514</td>
<td>$800,000</td>
<td>$763,016</td>
<td>($36,984)</td>
</tr>
<tr>
<td>2008</td>
<td>$150,000</td>
<td>$89,321</td>
<td>$60,679</td>
<td>$815,000</td>
<td>$785,906</td>
<td>($29,094)</td>
</tr>
<tr>
<td>2009</td>
<td>$150,000</td>
<td>$55,826</td>
<td>$94,175</td>
<td>$845,000</td>
<td>$796,123</td>
<td>($48,877)</td>
</tr>
<tr>
<td>2010</td>
<td>$150,000</td>
<td>$33,495</td>
<td>$116,505</td>
<td>$870,000</td>
<td>$820,007</td>
<td>($49,993)</td>
</tr>
<tr>
<td>2011</td>
<td>$150,000</td>
<td>$0</td>
<td>$150,000</td>
<td>$900,000</td>
<td>$844,607</td>
<td>($55,393)</td>
</tr>
</tbody>
</table>

Source: Berk & Associates, Black Lake Fire Department

In the case of BLFD laying off personnel due to the annexation, the City of Tumwater might not be legally obligated to hire staff previously working for FD 5 (RCW 35.13.225). As the City of Tumwater employs different hiring guidelines and standards related to training requirements for its paid and volunteer firefighters than does FD 5, former BLFD staff members seeking employment in the City would need to be able to meet these criteria in order to be considered eligible candidates.

**Response Time.** A third critical issue is BLFD’s ability to provide effective fire service protection to the remainder of residents living in FD 5. For example, a large rural area east of Black Lake lacks water hydrants. Traditionally, FD 5 has provided water tenders (trucks) to this area during fire-related calls. In the unlikely event that both fire stations in FD 5 were closed and the area was served exclusively by neighboring service providers, the next closest stations housing water tenders are located in FD 11 or FD 9. As municipalities do not typically own such equipment, Tumwater would be currently unable to provide such a service, which would result in the remaining FD 5 residents, most particularly those living in the northeastern strip, likely experiencing a significant increase in response time for water tenders. However, the City would likely purchase a tender or receive a tender in the asset distribution, and the City also has mutual aid contracts with other districts to help alleviate the tender shortage.

**FD 5 Levy**

FD 5 generates 96% of its revenue from a tax levy based on the assessed value of properties within the district. In 2006, FD 5 collected a total tax levy of $1.76 per $1,000 of assessed valuation, with $1.35 dedicated to the district’s operational fund and the remaining $0.41 collected to pay off general obligation bonds. The rapid population growth, increased value of residential and commercial property, and the limits imposed by the 2001 passage of I-747, have resulted in large budgetary constraints for the BLFD, as levy increases do not keep up with the current rate of inflation.

In response, the Board of Fire Commissioners of Thurston County adopted a resolution in 2006 concerning a proposition to increase the property tax levy set aside for expense funding to $1.50 per $1000 assessed value. The additional revenue would have been directed into the hiring of at least two more career firefighters, as well as providing emergency equipment upgrades and response
capability improvement. The proposition was placed on the November 6, 2006 ballot and was defeated by a margin of 52.3% to 47.7%. A recent increase in assessed valuation has further lowered the 2007 levy rate to $1.53 per $1,000 of assessed valuation, with $1.19 levied for operational funds and $0.34 levied to pay off previous debt.

WASHINGTON’S ASSET TRANSFER LAWS FOR FIRE DISTRICTS

State law guides the asset transfer among districts in the event of a change in governance, and it is useful to understand each situation as applicable to FD 5 after the proposed annexation. In practice, asset transfer agreements are subject to negotiation and rely on communication between the two governments. For more information, please reference the Municipal Research and Services Center of Washington’s (MRSC) Annexation Handbook, or RCW 35.02.190. The graphic below and text that follows explains how asset transfer works (Exhibit B-3).

Exhibit B-3
Asset Transfer: A Theoretical Example

<table>
<thead>
<tr>
<th>Fire District</th>
<th>If &gt;60% of PAA AV annexes...</th>
<th>If &lt;60%...</th>
<th>If &lt;5%...</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Transfers all assets &amp; liabilities to City</td>
<td>District continues to own assets; transfers % of AV to City</td>
<td>No payment occurs</td>
</tr>
<tr>
<td>City</td>
<td>City pays District for assets that remain in PAA</td>
<td>$</td>
<td>$</td>
</tr>
</tbody>
</table>

If 60% or more of the assessed real property valuation of a fire district is annexed to a city, the city will own all of the district’s assets. However, the city is to pay the district a sum equal to the percentage of the value of the real and personal property in the district that remains outside the annexed area. The payment is to be made within one year of the annexation, in cash, property, or contracts for fire protection services (RCW 35.02.190 and RCW 35A.14.380).

Residents in the fire protection district but outside the annexed area may hold an election to require the annexing city to assume responsibility for providing fire protection and for operating and maintaining district property, facilities, and equipment. In such a situation, the district must pay a reasonable fee to the city (or district) for the services it provides. If the fire district has ongoing general obligation indebtedness, the area being annexed will continue to pay its share of these costs until the bonds are fully repaid.

If less than 60% of the assessed real property valuation of a fire district is annexed to a city, the district maintains ownership of its assets. However, the district is to pay the city (in cash, properties, or contracts for fire protection services) a percentage of the value of its assets equal to the percentage of the value of the real property in the district that has been annexed into the city. This payment is to be made within one year, or within the time the district continues to collect taxes in the annexed area.
(RCW 35.02.200 and 35A.14.400). If the fire district has ongoing general obligation indebtedness, the area being annexed will continue to pay its share of these costs until the bonds are fully repaid.

If less than 5% of the area of the fire protection district is included in the area annexed, no payment is due the annexing city from the district, except in certain circumstances (RCW 35.02.205, RCW 35A.14.400). If the fire district has ongoing general obligation indebtedness, the area being annexed will continue to pay its share of these costs until the bonds are fully repaid.

If 100% of a fire protection district is included in the annexing city, all of the assets and liabilities of the district are to be transferred to the city upon annexation. The fire district in this case will be automatically dissolved.

**IMPLICATIONS OF STATE TRANSFER LAWS ON FD 5 WITH ANNEXATION**

The PAA make up 30% of FD 5’s assessed value. As less than 60% of the assessed real property valuation of FD 5 is being annexed to Tumwater, under Washington State Law, FD 5 maintains ownership of its assets. However, the District is to pay the City (in cash, properties, or contracts for fire protection services) a percentage of the value of its assets equal to the percentage of the value of the real property in the district that has been annexed into the city. This payment is to be made within one year, or within the time the district continues to collect taxes in the annexed area (RCW 35.02.200 and 35A.14.400).

While the PAA does not geographically incorporate any physical assets (for example fire stations or equipment) owned by FD 5, the District is still legally obligated to transfer 30 percent of its assets over to Tumwater. This is due to the fact that equipment and property are not owned by the fire department serving their districts, but rather by the residents who pay taxes for them. As such, the population living within the PAA has legal ownership of a portion of FD 5’s asset and will need to be compensated approximately $1,354,800 (Exhibit B-4).

It is important to highlight that this payment can be made in cash, property, or contracts for fire protection services, so the City of Tumwater and FD 5 would have discretion in resolving these asset transfer issues. An example of how these payments can be made can be found in examining pre-existing agreements, such as the one made by King County Fire District 25 and the City of Renton. In this particular agreement, the annexation of part of Fire District 25 by Renton resulted in a 10-year contract amount. The Fire District essentially “paid down” the total asset transfer amount over a period of time through a long-term contract with the City of Renton.
**Exhibit B-4**

**FD 5 Estimated Value of Assets (Stations, Apparatus, Cash Reserves)**

<table>
<thead>
<tr>
<th>Asset Value</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Station 51</td>
<td>$3,653,000</td>
</tr>
<tr>
<td>Station 52</td>
<td>$562,000</td>
</tr>
<tr>
<td>Storage Substation</td>
<td>$121,000</td>
</tr>
<tr>
<td>Cash</td>
<td>$180,000</td>
</tr>
<tr>
<td><strong>Total Before Asset Transfer</strong></td>
<td><strong>$4,516,000</strong></td>
</tr>
<tr>
<td><strong>30% Asset Transfer</strong></td>
<td><strong>$1,354,800</strong></td>
</tr>
<tr>
<td><strong>Total After Asset Transfer</strong></td>
<td><strong>$3,161,200</strong></td>
</tr>
</tbody>
</table>

Source: Berk & Associates, Black Lake Fire Department

**SCENARIOS**

While the City of Tumwater has expressed its intention to provide fire services to the PAA by its own fire department after annexation, several scenarios exist for FD 5 in providing services to the remainder of constituents living within District boundaries post-annexation. Washington State Law allows for a variety of governmental agreements between cities, towns, and fire districts, some of which will be discussed below:

**FD 5 Fully or Partially Merges with FD 9 or FD 11**

Agreement A and Agreement B outline the potential impacts of different merger agreements that FD 5 could enter into with one of the two districts located along its borders (FD 9 and FD 11):

**Agreement A.** FD 5 could fully merge with either FD 9 or FD 11 (RCW 52.06.010, RCW 52.06.150). Upon completion of the merger, BLFD would dissolve and transfer all paid firefighters, assets and revenue to the other District (9 or 11). The other District (9 or 11) would then assume sole responsibility of providing fire and emergency services to FD 5. Due to the strategic location of Fire Station 51, it is possible that the chosen merged District may decide to keep the station open to more effectively service residents living in FD 5 (such terms would need to be determined in the formal merger agreement).

**Agreement B.** FD 5 could enter a partial merger with FD 9 or FD 11 (RCW 52.06.090). In this scenario, the BLFD could transfer a portion of its paid firefighter staff, assets and revenue to the other District (9 or 11). Fire Station 52 could close and Station 51 would remain operational to serve residents living within close proximity. Both districts would need to negotiate the amount of coverage area, funding, staff, property, and equipment needed to each meet operational and financial specifications.

**City of Tumwater Provides All or Partial services to FD 5**

Currently the City of Tumwater and FD 5 have a Mutual Aid Agreement in which both respond to all fire-related emergency calls in FD 5 east of Black Lake (RCW 39.34.030). The City and District have the option of changing this agreement to state that Tumwater will assume sole responsibility of all or parts of FD 5 post annexation:
**Agreement A.** Under a service contract, the City of Tumwater would provide fire protection and EMS services to all of FD 5 after the proposed annexation. In this scenario, BLFD would terminate all paid firefighters, transfer the majority of its assets and revenue to the City. The City would determine the best service configuration using the combined stations of the two departments. Staff previously working for FD 5 would be eligible to work for the City’s fire department, although they would not be guaranteed a position. Both districts would need to negotiate the amount and method of payment needed to meet operational and financial specifications.

**Agreement B.** In this scenario, FD 5 would enter into a partial service contract with Tumwater (RCW 35A.11.040, RCW 52.12.031). Although Fire Station 52 would likely close, Station 51 could remain open with a functioning level of paid firefighters, volunteers, and additional staff. Tumwater FD would then provide coverage for a portion of FD 5 not as effectively covered by BLFD’s remaining station. In exchange for fire protection and EMS services by the City for a partial area of the District, FD 5 would need to agree upon the amount and type of the payment (i.e. assets, employees, and revenue) to be transferred over to the City. A few examples of this type of agreement can be found between the City of Enumclaw and King County FD 28 and the City of Puyallup and Pierce County FD 11.

**FD 5 Does Not Enter Into Any Contractual Agreement**

Another option is for the BLFD to continue providing its own services to all District residents. However, this alternative will pose a difficult task due to revenue shortages and reduction in assets after the proposed annexation. Even if one station remains operational (staffed with mostly volunteers and two or three paid firefighters), quickly and effectively responding to the needs of residents across the entire District does not appear to be a possibility due to the distance of Station 51 from residents living northeast and northwest of Black Lake.