Tax Increment Financing Project Analysis Review

– City of Kirkland –

March 27, 2023

Office of the Treasurer
State of Washington
Mike Pellicciotti

OFFICE OF THE TREASURER
STATE OF WASHINGTON
Mike Pellicciotti

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Kurt Triplett, City Manager
City of Kirkland
123 5th Avenue
Kirkland, WA 98033

Dear Mr. Triplett,

This letter confirms the Office of the State Treasurer's ("OST") receipt and review of the City of Kirkland's (the "City") revised tax increment financing ("TIF") project analysis, provided on March 6, 2023, and associated supplemental documents. OST and Piper Sandler, the state's municipal advisor, have reviewed the provided material. Based on our review, which is detailed in the sections to follow, we believe that the City's project analysis, supported by the supplemental documents, generally addresses the topics listed in section 020(2) of RCW 39.114 (the "TIF Statute").

Please note, this review is based on the information, projections, and assumptions provided by the City and its consultants in the project analysis and other supporting documents submitted by the City and its consultants. OST has not independently verified the data or its accuracy or performed any feasibility analyses or projections of its own.

Executive Summary

The proposed Tax Increment Area ("TIA") includes a portion of the Station Area east of I-405 of approximately 52.5 acres. The City is planning for land use and public improvements in the Station Area in connection with the voter-approved Sound Transit 3 ("ST3") transit funding package, which includes a reconfigured interchange and Bus Rapid Transit ("BRT") Stride station. The objective of the TIA, as described by the City's project analysis, is to leverage the BRT station regional transit investment to maximize transit-oriented development and create the most "Opportunity and Inclusion, Value for the City, Community Benefits, and Quality of Life."

The City's project analysis describes three public infrastructure projects to be financed by the TIA in order to encourage private development in the area. The total cost of these projects is estimated to be $58,000,000 in projected year-of-expenditure dollars and are scheduled to begin construction between 2023 and 2028. The project analysis prudently includes three development program scenarios ('Baseline', 'Reduced', and 'Core') to help assess potential risk based on different levels of private development within the TIA.

To finance the public infrastructure improvements, the City intends to issue Limited Tax General Obligation ("LTGO") bonds, which will be backed by the full faith and credit of the City. Should tax allocation revenues be insufficient to fully pay the debt service on the LTGO bonds, the full faith and credit pledge would require the City to pay the remaining debt service due on the bonds from the City's general revenues. As shown in Tables 3 and 4, the projections contained in the project analysis indicate that in each of the development program scenarios, the City will be required to pay some portion of the debt service due on the LTGO bonds from general revenues, especially in early years, due to projected shortfalls in tax allocation revenues.

In our review of the project analysis, one of our primary goals is to ensure that risks to the City are adequately disclosed. As we describe further below, in this proposed TIA, the primary risks to the City are lower-than-expected tax allocation revenues (due to delays in construction of the private development within the TIA) and lower-than-expected future assessed values in the TIA.

Statutory Role and Purpose of Review

As enacted by the 2021 Washington State Legislature, section RCW 39.114.020(7)(b) of the TIF Statute requires that prior to the adoption of an ordinance authorizing the creation of a TIA, the local government proposing the TIA must provide a project analysis to OST for review. OST must complete the review within 90 days of receipt of the project analysis. Upon completing the review, OST must promptly provide to the local government any comments regarding suggested revisions or enhancements to the project analysis that OST deems appropriate. OST received the first draft of the City's project analysis on November 18, 2022, and an updated project analysis was provided by the City to OST on March 6, 2023.

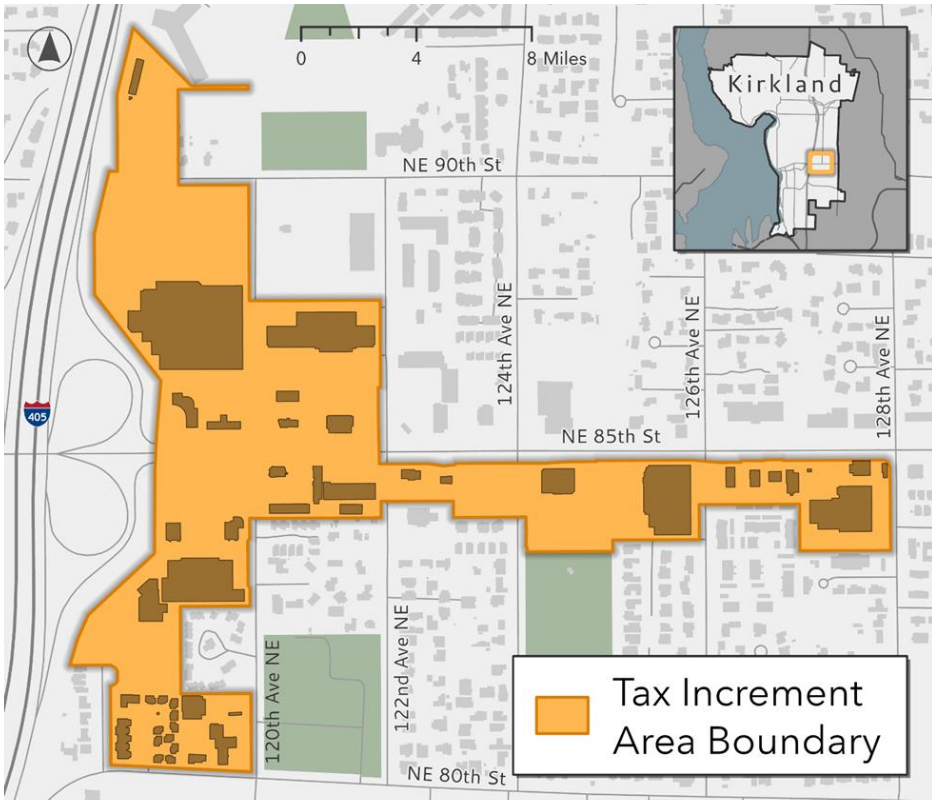
Project Team

Jurisdiction: City of Kirkland	**County:** King County
Project Title: NE 85th Street Station Area	**Redevelopment Area:** NE 85th Street Station Area
City of Kirkland: Kurt Triplett, City Manager Tracey Dunlap, Deputy City Manager (now retired) Michael Olson, Director of Finance & Admin. Sri Krishnan, Deputy Director of Finance & Admin. George Dugdale, Financial Planning Manager Kevin Pelstring, Financial Planning Supervisor Allison Zike, Deputy Planning & Building Director	**Consultants:** Bob Stowe, Stowe Development & Strategies Morgan Shook, ECONorthwest Deanna Gregory, Bond Counsel, Pacifica Law Group Stacey Crawshaw-Lewis, Bond Counsel, Pacifica Law Group Fred Eoff, Financial Advisor, PFM - Director Maggie Marshall, Financial Advisor, PFM - SMC

Proposed Tax Increment Area

The TIA includes a portion of the Station Area east of I-405 of approximately 52.5 acres, with blocks to the north and south of NE 85th Street (see Figure 1). The assessed valuation ("AV") of the TIA in 2022 is approximately $130,747,600 (about 0.35% of the City's total AV), which is less than the statutory limitations of the lesser of $200 million AV and 20% of the City's total AV ($36,947,748,933). According to the project analysis, the boundary represents key areas that are expected to be redeveloped over time, as the result of the infrastructure improvements funded by the TIA. Table 1 shows a list of parcels included in the proposed TIA.

Figure 1 – Map of Proposed Tax Increment Area



Source: City of Kirkland

Table 1 – Summary of TIF Parcels

Parcel ID	Appraised Land Value	Appraised Improvement Value	Total Appraised Value	Parcel ID	Appraised Land Value	Appraised Improvement Value	Total Appraised Value
1238500140	$2,863,600	$0	$2,863,600	1233100170	$2,184,100	$320,600	$2,504,700
1238500135	$834,600	$0	$834,600	1233100161	$385,000	$0	$385,000
1238500132	$1,349,600	$1,000	$1,350,600	1233100155	$1,412,400	$0	$1,412,400
1238500125	$2,463,200	$309,400	$2,772,600	1233100151	$1,280,200	$0	$1,280,200
1238500115	$8,210,900	$3,704,500	$11,915,400	1233100150	$1,335,300	$0	$1,335,300
6453600000	$137,000	$452,000	$589,000	1233100145	$5,429,000	$0	$5,429,000
4146790000	$112,700	$375,300	$488,000	1233100141	$1,280,200	$0	$1,280,200
1233100400	$3,048,400	$0	$3,048,400	1233100080	$1,023,100	$0	$1,023,100
1233100291	$635,300	$212,000	$847,300	1233100075	$1,280,400	$0	$1,280,400
1233100290	$1,443,000	$1,000	$1,444,000	1233100680	$7,452,400	$1,000	$7,453,400
1233100282	$780,800	$2,707,600	$3,488,400	1233100555	$1,497,800	$547,500	$2,045,300
1233100281	$2,077,300	$4,914,200	$6,991,500	1233100550	$0	$976,100	$976,100
1233100216	$1,040,400	$247,700	$1,288,100	1233100545	$1,775,400	$0	$1,775,400
1233100215	$1,922,300	$1,572,400	$3,494,700	1233100540	$1,922,100	$96,700	$2,018,800
1233100200	$1,280,200	$13,601,700	$14,881,900	1233100405	$3,593,000	$0	$3,593,000
1233100198	$1,280,200	$0	$1,280,200	1233100402	$3,438,200	$997,100	$4,435,300
1233100197	$1,280,200	$0	$1,280,200	1238500055	$1,846,100	$1,000	$1,847,100
1233100190	$1,321,700	$0	$1,321,700	1238500050	$2,997,400	$3,897,800	$6,895,200
1233100172	$490,000	$2,430,400	$2,920,400	1238500035	$16,546,200	$1,000	$16,547,200
1233100171	$372,000	$428,000	$800,000	1233100535	$1,648,200	$0	$1,648,200
1233100530	$1,681,700	$0	$1,681,700				
Total							$130,747,600

Source: City of Kirkland

Project Description

Public Improvements Within the TIA

In order to encourage the anticipated private development in the TIA, the project analysis identifies three infrastructure improvement projects that would support and help advance private redevelopment in the Station Area. These projects, described below, are expected to be funded with the proceeds of the LTGO bonds to be issued in connection with this TIA.

1) **NE 85th Street and I-405 Sewer Main Capacity Enhancements - $16,000,000**

   Construction of a new sewer main alignment to cross the I-405 along NE 90th Street and to improve the existing sewer line on NE 87th Street. Construction is anticipated in 2027-2028.

2) **Forbes Lake Park Development - $12,000,000**

   Forbes Lake Park is proposed to have an at least 10-foot wide boardwalk with connections to North Rose Hill Woodlands Park as well as active transportation facilities nearby. Construction is anticipated in 2028.

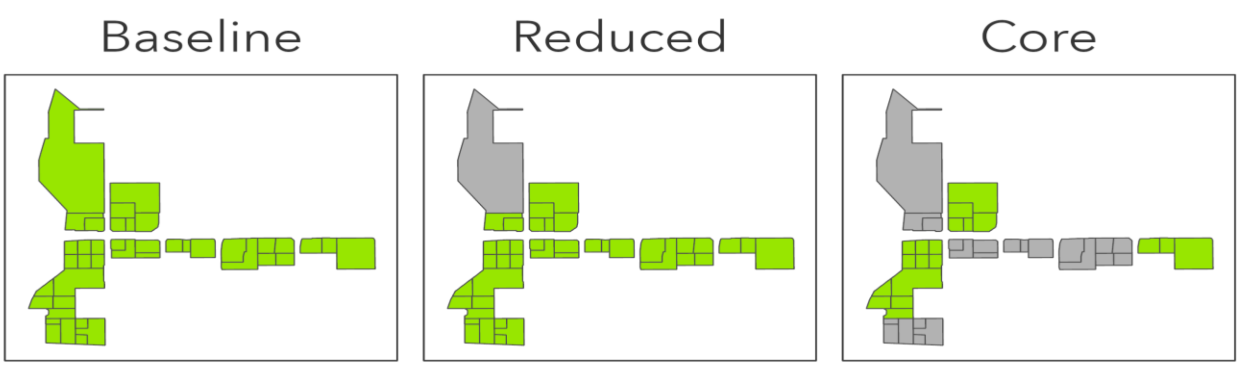
3) **124th Avenue NE Roadway Widening: NE 84th Lane to NE 90th Street - $30,000,000**

   Includes widening of 124th Avenue NE to five lanes and providing raised and protected bike lanes from NE 85th Street through the NE 90th Street intersection. This project also includes continuation of protected bike lanes south through the NE 85th Street intersection to NE 84th Lane to connect to exiting on-street bike lanes. Construction is anticipated in 2028-2029.

Private Development Within the TIA

The project analysis includes three development program scenarios to help assess potential risk based on different levels of private development within the TIA. Accordingly, the private development timeline varies depending on each scenario. Generally, it appears development is expected to begin in 2024 and continue through at least 2040, except for the 'Core' development program scenario, which has development continuing only through 2030. Figure 2 shows the developed sites under each scenario. The City has identified the 'Reduced' development program as the scenario most likely to occur.

Figure 2 – Map of Development Site Scenarios

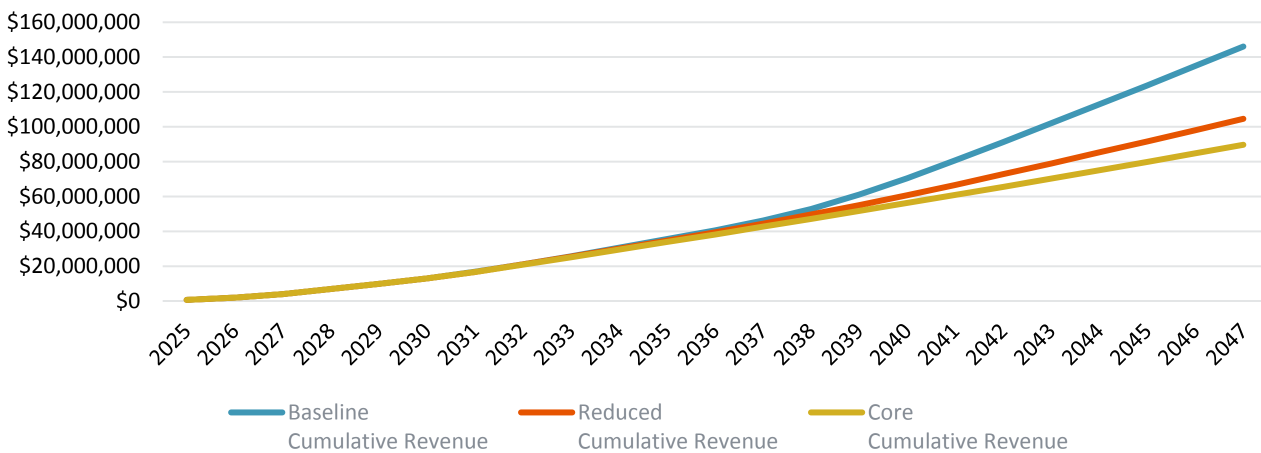


Source: City of Kirkland

Tax Allocation Revenue Projections

The project analysis indicates that the City will begin receiving tax allocation revenues in 2025. In terms of revenue projections, all three scenarios are identical through 2030 and do not materially differ until after 2035. In the 'Baseline' development program scenario, revenues are forecast to be $624,000 in 2025 (as with all three scenarios) and increase to over $11 million by 2047 (totaling $146,056,000 over the entire life of the TIA). Annual revenues for the 'Reduced' development program reaches $6.5 million in 2047 (total TIF revenue $104,572,000). Revenues in the 'Core' development program reaches $4,925,000 in 2047 (total TIF revenue $89,669,000).

Figure 3 – Cumulative TIF Revenue Projects



Source: City of Kirkland

Financing Plan

The City anticipates issuing $18 million of debt in early 2025 and $40 million of debt in early 2028 to fund the proposed infrastructure projects.[1] As stated in the project analysis, the City will need to service that debt with available resources regardless of whether the anticipated private development occurs, or assessed values increase, within the TIA. The City acknowledges that incremental revenues early in the TIF period may not be sufficient to service the debt; as private development construction will be in progress, it will take time to realize the incremental assessed value contributions that will ultimately determine the TIF allocation revenues estimated in their report. The debt is currently expected to be structured with level annual payments based on an estimated true interest cost of 4.50%.

The project analysis discusses the possibility of adjusting the timing and amount of debt issued based on development activity (i.e., delaying issuance, backloading debt, and/or use of capitalized interest). As such, it is possible that the City's issuance plans could change to better reflect progress in the development.

[1] Page 23 of the project analysis lists 2025 and 2028 as the bond issuance years, while information on page 27 lists different years. It is recommended that the City verify and correct this information.

Debt Capacity

Based on the City's total 2022 assessed value of $36,947,748,933, the City has $554,216,234 in total non-voted debt capacity (1.5% of 2022 AV). The City currently has $61,340,000 outstanding non-voted debt, leaving sufficient net non-voted debt capacity of $492,876,234 before the proposed $58,000,000 financing.

Table 2 – Debt Capacity

2021 Assessed Valuation for 2022 Collections	$36,947,748,933
Non-Voted Debt Capacity (1.5% of AV)	554,216,234
Less: Outstanding Non-Voted Debt	(61,340,000)
Remaining Non-Voted Debt Capacity	492,876,234
Less: Financing Proposed	(58,000,000)
Projected Remaining Non-Voted Capacity	**$434,876,234**
Projected Remaining Non-Voted Capacity %	**78.47%**

Source: City of Kirkland

Projected Debt Service Coverage

Depending on the pace and final features of the completed private development, the amount of shortfalls in tax allocation revenues compared to debt service that that the City will be required to fund varies greatly between the three development program scenario.

- In the 'Baseline' scenario, the City will be required to fund debt service revenue shortfalls in years 2025 through 2032 (excluding 2027) with general City revenues, with projections showing that it will be fully reimbursed for these payments by the end of 2039.
- In the 'Reduced' scenario, the revenue shortfalls extend through 2033, with the City being fully reimbursed by the end of 2042.
- For the 'Core' scenario, the revenue shortfalls extend through 2037, with City being fully reimbursed by the end of 2047.

Tables 3 and 4 below summarize the total tax allocation revenues, annual surpluses and deficits, and debt service coverage for the three development program scenarios.

Table 3 – Tax Allocation Revenues and Debt Service Coverage

Development Program	First Year Tax Allocation Revenues Exceed TIF Debt Service[1]	Year That Allocation Revenues Fully Reimburse Debt Service Shortfalls	Total Projected TIF Revenue	Total Projected TIF Debt Service	Projected Maximum Cumulative Shortfall	Total Surplus/ (Shortfall)	Average Debt Service Coverage Ratio
Baseline	2033	2039	$146,056,000	$89,180,000	($5,429,000)	$56,876,000	1.66x
Reduced	2034	2042	$104,572,000	$89,180,000	($5,518,000)	$15,392,000	1.19x
Core	2038	2047	$89,669,000	$89,180,000	($6,106,000)	$489,000	1.02x

1. *Revenues exceed debt service in 2027 during the reduced debt service period.*

Source: City of Kirkland

Table 4 – TIF Debt Service Coverage

Baseline

Year	TIF Revenues	TIF Debt Service	Surplus (Shortfall)	Cumulative Surplus (Shortfall)	TIF DSC
2025	624,000	1,384,000	(760,000)	(760,000)	0.45x
2026	1,282,000	1,384,000	(102,000)	(862,000)	0.93x
2027	2,062,000	1,384,000	678,000	(184,000)	1.49x
2028	2,839,000	4,459,000	(1,620,000)	(1,804,000)	0.64x
2029	2,996,000	4,459,000	(1,463,000)	(3,267,000)	0.67x
2030	3,171,000	4,459,000	(1,288,000)	(4,555,000)	0.71x
2031	3,739,000	4,459,000	(720,000)	(5,275,000)	0.84x
2032	4,305,000	4,459,000	(154,000)	(5,429,000)	0.97x
2033	4,612,000	4,459,000	153,000	(5,276,000)	1.03x
2034	4,925,000	4,459,000	466,000	(4,810,000)	1.10x
2035	4,977,000	4,459,000	518,000	(4,292,000)	1.12x
2036	5,029,000	4,459,000	570,000	(3,722,000)	1.13x
2037	5,552,000	4,459,000	1,093,000	(2,629,000)	1.25x
2038	6,658,000	4,459,000	2,199,000	(430,000)	1.49x
2039	8,240,000	4,459,000	3,781,000	3,351,000	1.85x
2040	9,490,000	4,459,000	5,031,000	8,382,000	2.13x
2041	10,157,000	4,459,000	5,698,000	14,080,000	2.28x
2042	10,616,000	4,459,000	6,157,000	20,237,000	2.38x
2043	10,728,000	4,459,000	6,269,000	26,506,000	2.41x
2044	10,841,000	4,459,000	6,382,000	32,888,000	2.43x
2045	10,955,000	3,075,000	7,880,000	40,768,000	3.56x
2046	11,071,000	3,075,000	7,996,000	48,764,000	3.60x
2047	11,187,000	3,075,000	8,112,000	56,876,000	3.64x
Total[1]	146,056,000	89,180,000	56,876,000		1.66x

Reduced

Year	TIF Revenues	TIF Debt Service	Surplus (Shortfall)	Cumulative Surplus (Shortfall)	TIF DSC
2025	624,000	1,384,000	(760,000)	(760,000)	0.45x
2026	1,282,000	1,384,000	(102,000)	(862,000)	0.93x
2027	2,062,000	1,384,000	678,000	(184,000)	1.49x
2028	2,839,000	4,459,000	(1,620,000)	(1,804,000)	0.64x
2029	2,996,000	4,459,000	(1,463,000)	(3,267,000)	0.67x
2030	3,171,000	4,459,000	(1,288,000)	(4,555,000)	0.71x
2031	3,717,000	4,459,000	(742,000)	(5,297,000)	0.83x
2032	4,261,000	4,459,000	(198,000)	(5,495,000)	0.96x
2033	4,436,000	4,459,000	(23,000)	(5,518,000)	0.99x
2034	4,615,000	4,459,000	156,000	(5,362,000)	1.03x
2035	4,664,000	4,459,000	205,000	(5,157,000)	1.05x
2036	4,712,000	4,459,000	253,000	(4,904,000)	1.06x
2037	4,997,000	4,459,000	538,000	(4,366,000)	1.12x
2038	5,287,000	4,459,000	828,000	(3,538,000)	1.19x
2039	5,384,000	4,459,000	925,000	(2,613,000)	1.21x
2040	5,591,000	4,459,000	1,132,000	(1,481,000)	1.25x
2041	5,933,000	4,459,000	1,474,000	(7,000)	1.33x
2042	6,170,000	4,459,000	1,711,000	1,704,000	1.38x
2043	6,235,000	4,459,000	1,776,000	3,480,000	1.40x
2044	6,300,000	4,459,000	1,841,000	5,321,000	1.41x
2045	6,365,000	3,075,000	3,290,000	8,611,000	2.07x
2046	6,432,000	3,075,000	3,357,000	11,968,000	2.09x
2047	6,499,000	3,075,000	3,424,000	15,392,000	2.11x
Total[1]	104,572,000	89,180,000	15,392,000		1.19x

Core

Year	TIF Revenues	TIF Debt Service	Surplus (Shortfall)	Cumulative Surplus (Shortfall)	TIF DSC
2025	624,000	1,384,000	(760,000)	(760,000)	0.45x
2026	1,282,000	1,384,000	(102,000)	(862,000)	0.93x
2027	2,062,000	1,384,000	678,000	(184,000)	1.49x
2028	2,839,000	4,459,000	(1,620,000)	(1,804,000)	0.64x
2029	2,996,000	4,459,000	(1,463,000)	(3,267,000)	0.67x
2030	3,171,000	4,459,000	(1,288,000)	(4,555,000)	0.71x
2031	3,695,000	4,459,000	(764,000)	(5,319,000)	0.83x
2032	4,216,000	4,459,000	(243,000)	(5,562,000)	0.95x
2033	4,260,000	4,459,000	(199,000)	(5,761,000)	0.96x
2034	4,305,000	4,459,000	(154,000)	(5,915,000)	0.97x
2035	4,350,000	4,459,000	(109,000)	(6,024,000)	0.98x
2036	4,395,000	4,459,000	(64,000)	(6,088,000)	0.99x
2037	4,441,000	4,459,000	(18,000)	(6,106,000)	1.00x
2038	4,488,000	4,459,000	29,000	(6,077,000)	1.01x
2039	4,534,000	4,459,000	75,000	(6,002,000)	1.02x
2040	4,581,000	4,459,000	122,000	(5,880,000)	1.03x
2041	4,629,000	4,459,000	170,000	(5,710,000)	1.04x
2042	4,677,000	4,459,000	218,000	(5,492,000)	1.05x
2043	4,726,000	4,459,000	267,000	(5,225,000)	1.06x
2044	4,775,000	4,459,000	316,000	(4,909,000)	1.07x
2045	4,824,000	3,075,000	1,749,000	(3,160,000)	1.57x
2046	4,874,000	3,075,000	1,799,000	(1,361,000)	1.59x
2047	4,925,000	3,075,000	1,850,000	489,000	1.60x
Total[1]	89,669,000	89,180,000	489,000		1.02x

1. *Total row for debt service coverage reflects average coverage ratio.*
2. *Assumes interest rate of 4.50%.*

Source: City of Kirkland

City of Kirkland Financials

The City provided information summarizing the funds available to pay LTGO debt service for the past five years, primarily consisting of General Fund and Excise Capital Improvement Fund monies. These combined funds produced a surplus in all five years, with net revenues ranging from $27 million to $40 million. A portion of these funds appear to have been utilized to fund capital projects in the past; however, these funds could be reprogrammed towards the payment of debt service, if necessary. The TIF debt service projections show maximum annual debt service of $4,459,000.

The City's General Fund balance, including the Excise Capital Improvement Fund, has totaled around $100 million annually (just over 100% of annual expenditures, excluding capital). In the most conservative development program scenario, the City projects a cumulative deficit in tax allocation revenues of just over $6.1 million, or 5.6% of the City's 2021 ending General Fund balance.

In the event of a temporary or long-term tax allocation revenue shortfall, the City's fund balances, or other current capital projects, may be negatively impacted.

Table 6 – Revenue Available for Debt Service

		2017	2018	2019	2020	2021
Beg. Balance						
	General Fund	46,138,892	50,560,881	61,091,511	74,002,754	81,101,362
	Excise CIP	21,785,577	25,062,775	24,397,555	12,833,492	19,344,453
	Debt Service Fund	331,708	347,643	356,525	373,074	925,859
	Total	**68,256,177**	**75,971,299**	**85,845,591**	**87,209,320**	**101,371,674**
Revenue						
	General Fund	108,137,634	117,588,709	125,703,639	131,875,806	138,274,477
	Excise CIP	10,575,074	12,460,244	15,982,701	13,346,869	17,839,679
	Debt Service Fund	1,604,877	1,586,012	1,565,131	1,343,071	1,042,905
	Total	**120,317,585**	**131,634,965**	**143,251,471**	**146,565,746**	**157,157,061**
Expenditures						
	General Fund	93,131,793	99,661,402	103,190,314	114,331,518	117,333,422
	Excise CIP					
	Debt Service Fund					
	Total	**93,131,793**	**99,661,402**	**103,190,314**	**114,331,518**	**117,333,422**
Income Above Expenditures		27,185,792	31,973,563	40,061,157	32,234,228	39,823,639
Total Revenue Available	**Total**	**95,441,969**	**107,944,862**	**125,906,748**	**119,443,548**	**141,195,313**
Debt Service		4,147,909	4,127,343	4,101,747	4,075,708	3,536,211
Other Inflows (Outflows)						
	General Fund	(11,781,353)	(7,396,677)	(11,876,677)	(10,445,681)	(14,497,380)
	Excise CIP	(7,297,877)	(13,125,464)	(27,546,764)	(6,835,908)	(16,387,640)
	Debt Service Fund	2,558,967	2,550,213	2,553,165	3,285,422	2,500,569
	Total	**(16,520,263)**	**(17,971,928)**	**(36,870,276)**	**(13,996,167)**	**(28,384,451)**
Ending Balance						
	General Fund	49,363,380	61,091,511	71,728,158	81,101,362	87,545,037
	Excise CIP	25,062,775	24,397,555	12,833,492	19,344,453	20,796,493
	Debt Service Fund	347,643	356,525	373,074	925,859	933,123
	Total	**74,773,798**	**85,845,591**	**84,934,724**	**101,371,674**	**109,274,653**
Restricted Funds						
	Non-spendable	443,551	743,419	839,775	819,265	871,068
	Drug Enforcement	116,072	393,670	148,975	100,286	74,397
	Fire Interlocal	130,753	252,787	130,702	124,424	159,334
	Prop one			345,943	888,783	751,530
	Fire pension	1,197,501	1,306,638	1,264,218	1,306,682	1,292,976
	Committed ARCH				4,696,369	2,266,988
	Total	**1,887,877**	**2,696,514**	**2,729,613**	**7,935,809**	**5,416,293**
Ending Available for Debt Service		**72,885,921**	**83,149,077**	**82,205,111**	**93,435,865**	**103,858,360**

Source: City of Kirkland

Key Risks to the City

From our review of the project analysis, it appears that the project will provide significant benefit to the City and region. Nonetheless, the project comes with certain risks to the City, primarily related to the construction timeline for public improvements within the TIA and the sufficiency of projected tax allocation revenues to repay LTGO bonds that the City expects to issue to finance public infrastructure improvements.

During years with shortfalls, the City will be required to pay any difference between debt service due and tax allocation revenues received from general City revenues. While the City plans to reimburse itself for such debt service payments made from general City revenues, it is important for decision makers to be aware of the potential magnitude and timing of such payments and reimbursements and, since the TIF legislation limits the ability to collect tax allocation revenues to a period of 25 years, delays could also reduce the overall amount of tax allocation revenues that would be received by the City. Additional factors that could impact tax allocation revenues are described below:

> *Escalation of Project Costs:* With public improvements projected to be completed from 2027 through 2029, inflation could have a significant impact on the projected cost of these projects. However, this is somewhat mitigated by the inclusion of a 30% contingency in the projections. The project analysis shows cost inflation for the projects of approximately 4.00% - 5.00% per annum. According to Mortenson's Third Quarter 2022 report, construction cost inflation for Seattle was 9.3% YoY.
>
> *Permits*: Unforeseen delays in permits could negatively impact the construction of the expected residential, commercial, and mixed-use properties within the TIA. Delays to either the public improvements or the private developments could negatively impact the timing and/or amount of tax allocation revenues.
>
> *Economic Conditions*: The timing of tax allocation revenues could be negatively impacted by a downturn in the economy. The planned development is multi-faceted with commercial, mixed-use, multi-family residential, and office components. Given the diversity in product type, a variety of economic factors could negatively impact the timeline and ultimate demand for development, jeopardizing the rate and scale of private development and reducing potential tax allocation revenues.
>
> *Construction Delays*: Any setback or delay in the private developers' ability to complete construction projects could harm tax allocation revenues. Whether the cost of the improvements themselves or some unforeseen change in developers' abilities to complete both their public improvements and private developments, the City will remain responsible for repaying the LTGO bonds issued for the project, once issued. Moreover, any delay in the City's ability to complete the public improvements necessary for private developers to close on contracts or initiate private developments exposes the project to risk of delayed timing and/or a reduced amount of tax allocation revenues.
>
> *Assessed Valuations*: As private developments are completed, tax allocation revenues may be less than anticipated if the assessed value projections do not materialize or take more time to fully hit the tax rolls than is currently projected. If assessed valuations come in lower than or later than expected, projected tax allocation revenues would be reduced.

Interest Rate Risk: The City is exposed to interest rate risk until its bonds are sold. The key assumption of a 4.5% interest rate for the LTGO bonds offers a slight cushion to current market conditions. However, in the event that interest rates rise to levels in excess of this assumption, debt service will exceed the amounts assumed in the project analysis.

Risk Summary: The general impact to the City if any of the risk factors outlined above are realized could be a greater reliance on the City's general revenues to pay the debt service on the LTGO bonds issued to fund public improvements in the TIA. Potential negative cashflows during these periods of time will require the City to use general City revenues or reserves. If tax allocation revenues end up being lower than expected, it will force the City to apply more of its available funds towards the repayment of the LTGO bonds, reducing the City's ability to allocate those funds to other projects or operations. Likewise, if tax allocation revenues end up being lower than expected, the City is also at risk of not being fully reimbursed from tax allocation revenues for any debt service payments that were made from general revenues.

Recommendations

The NE 85th Street Station Area Development is a significant long-term and large-scale project. To help ensure the long-term financial success of the project and to minimize risk, we recommend the City continuously monitor the risks identified and consider the following measures.

1. We recommend that the City discuss how much risk exposure is appropriate for the project and how much potential debt service costs it is willing to cover to advance the project through years of tax allocation revenue shortfalls.

2. Based on the City's willingness to cover potential debt service costs, we recommend the City consider budgeting for and setting aside funds to cover potential tax allocation revenue shortfalls.

3. As the project moves forward, coordinate closely with the King County Assessor's Office to help ensure that the tax allocation revenue projections match the County's assessment process and are as realistic as possible.

4. The City's interest rate assumptions contain only a small amount of cushion compared to current market conditions. We recommend that the City consider using somewhat more conservative interest rate assumptions, especially if the issuance of the bonds extends into 2028.

5. Given that the revenue projections through 2030 are identical for the three development program scenarios, we recommend performing additional analysis to refine the impact of delays in development occurring prior to 2030.

6. We recommend the City revisit public improvement cost projections frequently and utilize a publicly recognized inflation index to inform inflation projections.

7. The City should note that page 27 of the project analysis dated March 6, 2023 references bond issuance dates of 2024 and 2026, whereas pages 22 and 28, along with the debt service tables, reflect issuances in 2025 and 2028.

Thank you for the opportunity to review the City's TIA project analysis. Based upon the information provided to date in connection with this project, this concludes our review. If there are material changes in the scope, timing, or cost of the project, please let us know. We wish the City all the best with the project.

Respectfully,

Mike Pellicciotti
Washington State Treasurer

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Jason Richter
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