



CITY AUDITOR 345 6th Street, Suite 600, Bremerton, WA 98337-1873 & Phone (360) 473-5369

June 20, 2017

To: Audit Committee Members:

Pat Sullivan, Audit Committee Chair and Council Member
Deborah McDaniel, Audit Committee Vice-Chair
Eric Younger, CPA, Council President
Dennis Treger, CPA, Audit Committee Member
Anthony Hillman, CPA, Audit Committee Member

Re: Connection Credit Union Lease History Review

Dear Audit Committee Members:

At your request and based on the information reviewed to date, I am submitting a report summarizing my review of the Connection Credit Union (“CCU”) lease history. The current lease expires August 31, 2017 and renewal of this agreement requires City Council (“Council”) approval. I was asked to summarize the lease history and contract terms and provide a report intended to assist Council in its contract renewal deliberations.

My work included the consideration and/or analysis of certain records including:

1. [Lease agreements between the City of Bremerton \(“City”\) and CCU for the following terms:](#)
 - a. September 1, 2011 to August 31, 2012,
 - b. August 21, 2012 to August 31, 2014, and
 - c. September 1, 2014 to August 31, 2017;
2. [2017 lease agreement between Kitsap County and CCU for the Port Orchard branch;](#)
3. [Connection Credit Union 2016 Annual Report;](#) and
4. Miscellaneous research.

Additionally, I relied on information provided by Scott Prior, the CCU President and CEO.

CCU BACKGROUND

CCU was founded by the employees of the City of Bremerton in 1958 as the City of Bremerton Employees Credit Union. There were 32 original members who invested \$5 each, yielding total assets of \$160. Over time, CCU expanded by adding City of Port Orchard employees, Kitsap County employees and merging with another small credit union. In 2006, membership was opened to anyone who lives, works, worships or attends school in Kitsap County and the name was changed to Connection Credit Union. CCU had \$30.8 million in assets at the end of 2016. (Mr. Prior stated the next largest local credit union is Kitsap Credit Union, which has approximately \$1 billion in assets.)



CCU markets itself as community and family-oriented, and valuing its loyal members. Its vision is, "Helping members build financial futures, one relationship at a time." CCU has a branch in each of the following locations: Silverdale, Port Orchard, and Bremerton.

In addition to serving its members, CCU provides services to other credit union members through shared branching, a national network of credit unions from all over the country that share facilities to give members thousands of locations to make transactions.

CCU BREMERTON BRANCH

The agenda bill for the August 17, 2011 City Council meeting indicates that CCU had a presence in downtown Bremerton from 1958 until approximately 2008. In August 2011, CCU wanted to re-establish its presence in downtown Bremerton and the City agreed to lease CCU 72 square feet of space within the Bremerton Fire Department Station No. 1. The space CCU occupies is where the Fire Department receptionist was situated before the position was eliminated several years prior. In addition to the 72 square feet, CCU may schedule access to and use common areas of the property such as the kitchen area, conference room and training room.

The only signage for the Bremerton location is a small sandwich board (maybe two feet high) on the sidewalk in front of the fire station. It is highly unlikely that anyone driving by will notice the credit union unless they know it is there. Even inside the fire station lobby, the credit union space is not immediately noticeable. The CCU Member Service Representative's desk nearly fills CCU's entire rented space. Please refer to the attached photos (2).

As of May 15, 2017, 96 of the 334 City employees that receive their pay via direct deposit have at least one CCU account. Additionally, 11 of 42 LEOFF 1 retirees that are paid via direct deposit have at least one CCU account. In total, over 28 percent of City employees and LEOFF 1 retirees bank at CCU.

The CCU Member Service Representative stated the Bremerton branch can get quite busy. On Fridays she serves as many as 100 members. A member came in during my brief visit.

The Fire Chief, David Schmitt, stated there is additional foot traffic through the fire station, and increased usage of the parking lot and restrooms, which is to be expected. Chief Schmitt also stated that in addition to their leased space, bank staff have a vault in a back room; use of the back room is not specified in the lease. Chief Schmitt has no major concerns with having CCU in the fire station lobby and is agreeable to renewing the lease. If appropriate, Chief Schmitt would like the rent increased.

BREMERTON LEASE TERMS

Monthly rent for the CCU space in the Bremerton fire station lobby was initially \$350. In the ensuing lease agreements, monthly rent was increased to \$360 and \$375, with each lease providing for annual increases based on 100 percent of the Seattle/Tacoma/Bremerton CPI-W. The current rent is \$389.77, which is \$64.96 per square foot annually. The advertised rent for office space in downtown Bremerton ranges primarily from \$10 to \$14 per square foot annually. In addition to rent, CCU pays monthly leasehold excise tax of \$50.05 to the



City. Utilities and normal maintenance and repairs, for which the CCU incremental cost is de minimis, are paid by the City. Either party can terminate the lease with 60-day notice.

PORT ORCHARD LEASE TERMS

CCU rents 350 square feet from Kitsap County in the Givens Community Center in Port Orchard. The monthly rent for this space is \$100, or \$3.43 per square foot annually. Utilities are paid by the County. Mr. Prior stated CCU has been at this space since about 2002.

SILVERDALE BRANCH

CCU owns the Silverdale branch building. County records indicate this building is over 4,200 square feet. This is CCU's main branch.

FINANCIAL SUMMARY

During 2015 and 2016, CCU had approximately \$2 million dollars of annual gross income with over 80 percent from interest on loans. Expenses totaled approximately \$1.9 million dollars each year with labor expense being the biggest expense totaling just under 40 percent of income. Income before dividends was approximately \$30,000 in 2015 and \$94,000 in 2016. Dividends paid to the members totaled about \$20,000 each year. The table below summarizes CCU's income and expenses from 2015 and 2016:

Description	2015		2016		Difference
	Amount	% of Income	Amount	% of Income	
Income:					
Interest on loans	\$ 1,677,073	84.0%	\$ 1,664,644	81.7%	\$ (12,429)
Income on investments	24,464	1.2%	49,512	2.4%	25,048
Other income	294,894	14.8%	322,286	15.8%	27,392
Total income	\$ 1,996,431 [▼]	100.0%	\$ 2,036,442	100.0%	\$ 40,011
Expenses:					
Employee compensation and benefit:	\$ 747,010	37.4%	\$ 806,077	39.6%	\$ 59,067
Professional and outside services	315,267	15.8%	324,315	15.9%	9,048
General office expense	215,771	10.8%	224,032	11.0%	8,261
All other expenses	688,565	34.5%	588,193	28.9%	(100,372)
Total expenses	\$ 1,966,613 [▼]	98.5%	\$ 1,942,617	95.4%	\$ (23,996)
Income before dividends	\$ 29,818 [▼]	1.5%	\$ 93,825	4.6%	\$ 64,007
Dividends	\$ 18,840	0.9%	\$ 20,441	1.0%	\$ 1,601
Net income	\$ 10,978 [▼]	0.5%	\$ 73,384	3.6%	\$ 62,406



SUMMARY

The City is generating rental income with almost no associated expense by leasing space that might otherwise be underutilized. This lease arrangement appears to be a good model for efficiently utilizing City assets.

It may be appropriate to update the lease to reflect CCU's usage of the back room for its vault.

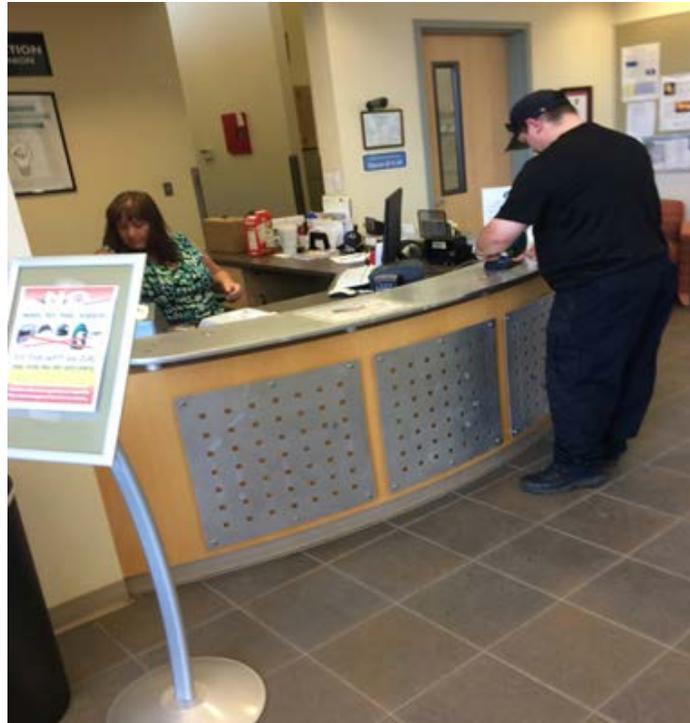
Please contact me if you have questions or need additional information.

Sincerely,

Jennifer L. Sims CPA/CFF, CFE
City Auditor

cc: Mayor Lent
David Schmitt, Fire Chief
DeWayne Pitts, CPA, CFE, Finance Director
Mike Riley, Assistant Finance Director

PHOTOS



Direct view of service counter



View from entrance at Fire Station No. 1