ECONOMIC AND REVENUE FORECAST

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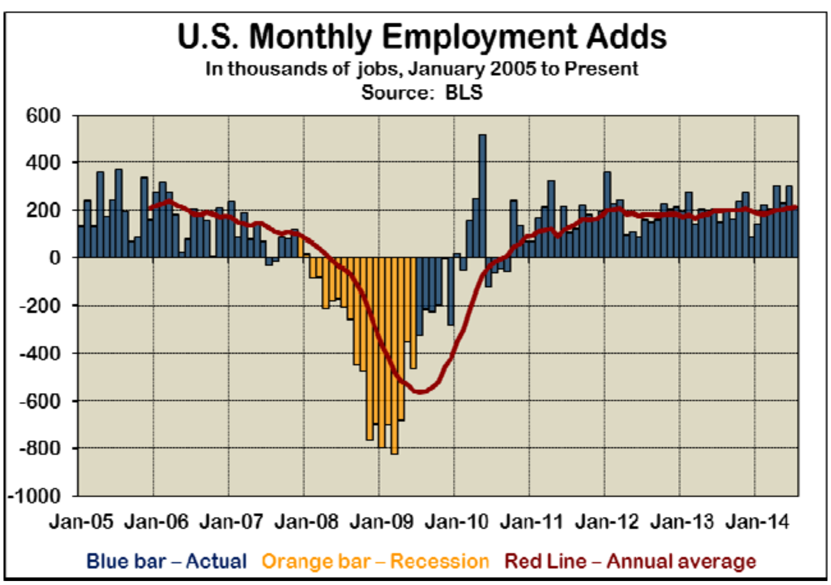
This section addresses the key economic issues underlying the King County budget and identifies the major revenue sources for all county funds. The section includes 1) a discussion of the national and regional economy and forecast, 2) a series of indicators describing the cost of King County government, 3) a description of the King County revenue forecast and major revenue sources, and 4) a synopsis of the General Fund financial plan. Additional economic and forecasting information is available through the King County Office of Economic and Financial Analysis (OEFA).[1]

Most County revenue sources are sensitive to the performance of the economy such as changes in income, employment, property values, inflation, and real estate transactions. For example, sales tax revenues are largely driven by income, inflation and employment. When these factors rise, sales tax receipts increase. Similarly, County expenditure projections are directly tied to inflation forecasts since a significant portion of county costs are directly tied to the local Consumer Price Index (CPI). The following section describes the current outlook for the national and local economies, and presents detail on forecasts for revenues supporting County funds. The fund summary for the General Fund is also located in this section, while descriptions of the appropriation units within the General Fund are located throughout the budget document.

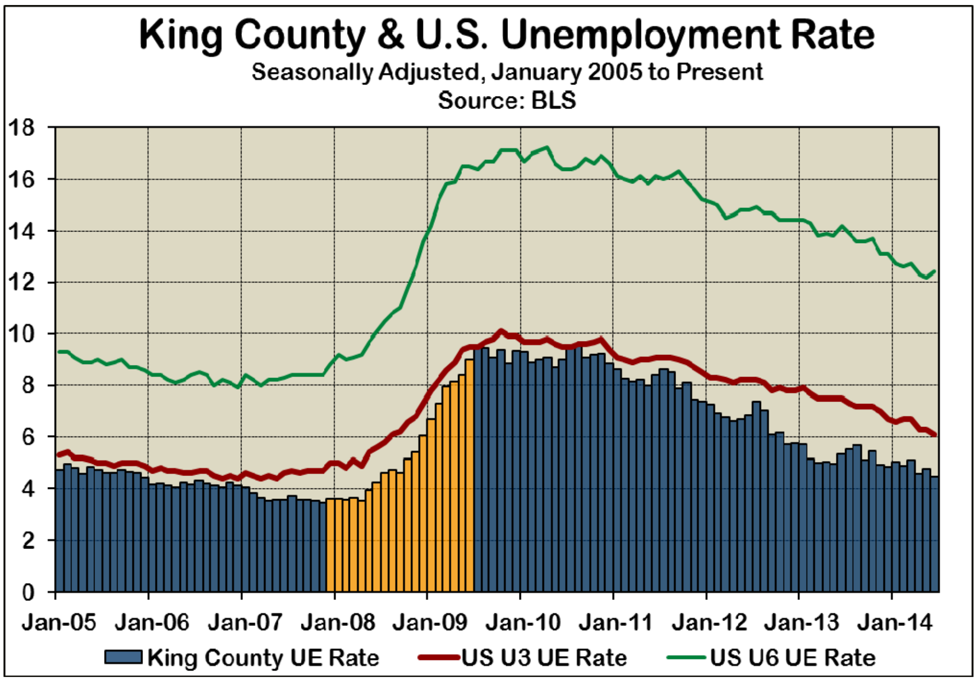
1. The National and Regional Economy

The U.S. economy has been expanding since the end of the recession in June of 2009, but the rate of growth has been low by historic standards. The average annual growth in Gross Domestic Product (GDP) has been less than 2% compared with a long run average rate of growth of about 3.2%. Because of this slow economic growth, employment growth has also been slow, averaging 119,000 new non-farm jobs each month through the end of 2013. However, forecasts for economic growth for 2014 and beyond are optimistic citing continued recovery in housing, household balance sheets and the resolution of many of the fiscal issues that acted to constrain growth. Despite economic contraction in the first quarter of 2014 (largely due to severe winter weather), GDP grew by more than 4% over the year in the second quarter while employment additions in 2014 have averaged 230,000 per month through July. The chart below plots monthly additions to non-farm employment in the U.S.



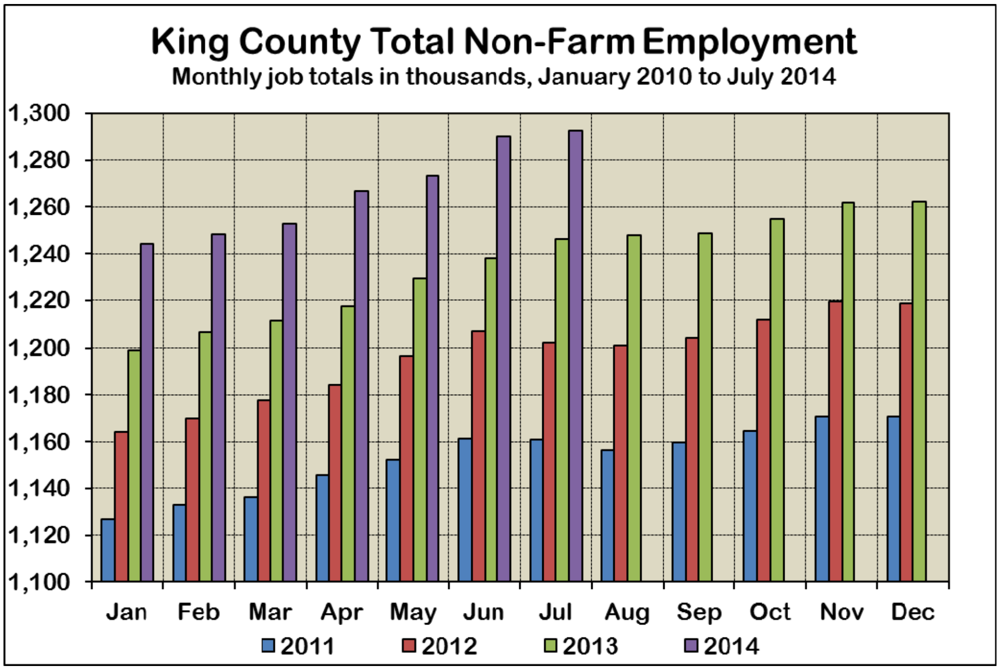
[1] OEFA's website is http://www.kingcounty.gov/business/Forecasting.aspx.

The unemployment rate peaked in October 2009 at 10% and has generally been falling as indicated in the chart below. As of July 2014, there were 9.7 million unemployed workers and the unemployment rate was 6.2%. The red line is U.S. unemployment as is typically presented (the "U3" rate). Some, including members of the Federal Reserve, have noted that the headline unemployment rate may not be performing well as an indicator of labor market slack. They cite the elevated level of part-time workers as an example of how labor markets are not performing as well as would be desired, and note that we should be considering other indicators when assessing the state of U.S. labor markets. So a more inclusive measure of unemployment (the "U6" rate) is also plotted below which includes workers that are employed part-time but would prefer to be working full time and those that want to work but that have not looked in the last four weeks ("marginally attached workers"). As can be seen the U6 measure is elevated relative to the U3 measure compared with the period before the 2007-2009 recession.

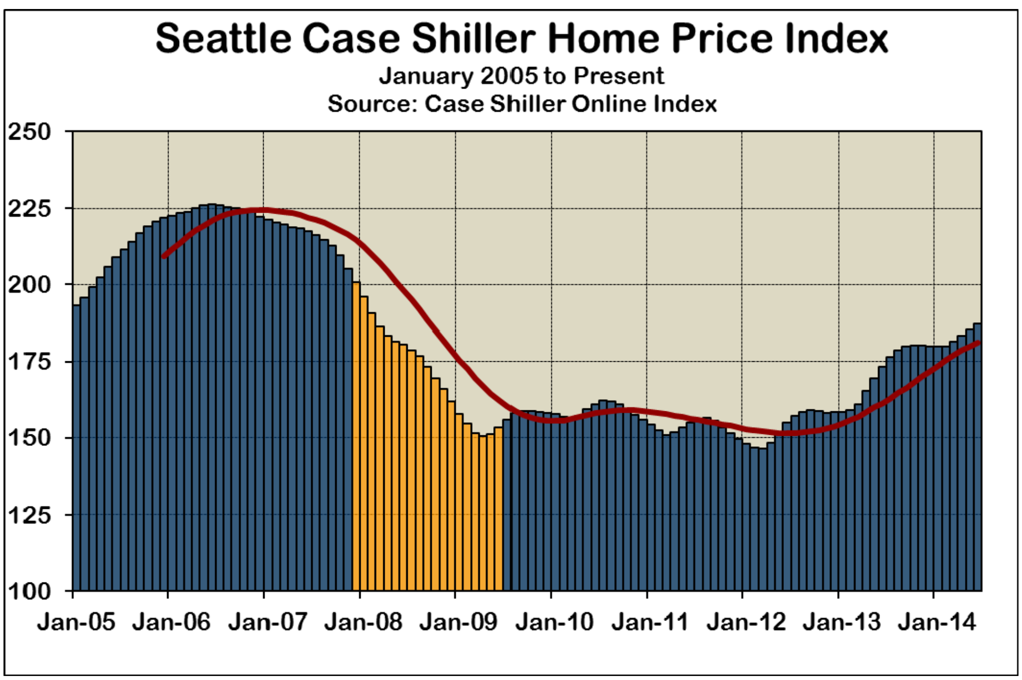


Other economic indicators show improvement in the national economy. Household net worth continues to recover due to increasing housing values and the strong performance of financial markets. Forecasts for the U.S. economy include accelerating GDP growth in 2014 and 2015, relatively modest inflation and a slow drop in the unemployment rate. Risks to the forecast include a slowdown in China, turmoil in the Middle East and fiscal policy decisions to be made in 2015 regarding the debt limit and the federal budget.

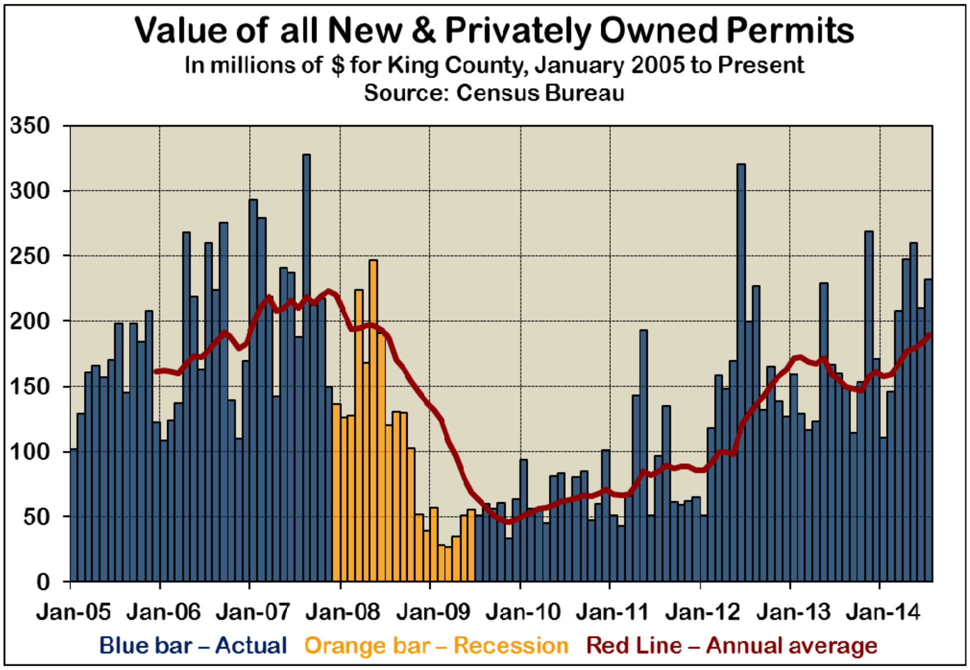
The chart above also highlights that the King County economy has performed better through the recession and recovery than the U.S. economy. The unemployment rate in King County has generally been below the national rate throughout the recession and recovery and has fallen at a faster pace recently. The unemployment rate in King County was 4.9% in July 2014, whereas the U.S. unemployment rate was 6.2%. This low unemployment rate largely reflects the strong job growth in the county. The chart below presents King County employment levels by month since 2010. Non-farm employment has been growing significantly in King County, with increases of 3.7% in the first half of 2014. The employment level in King County is now greater than the level of employment the county experienced prior to the 2007-2009 recession.



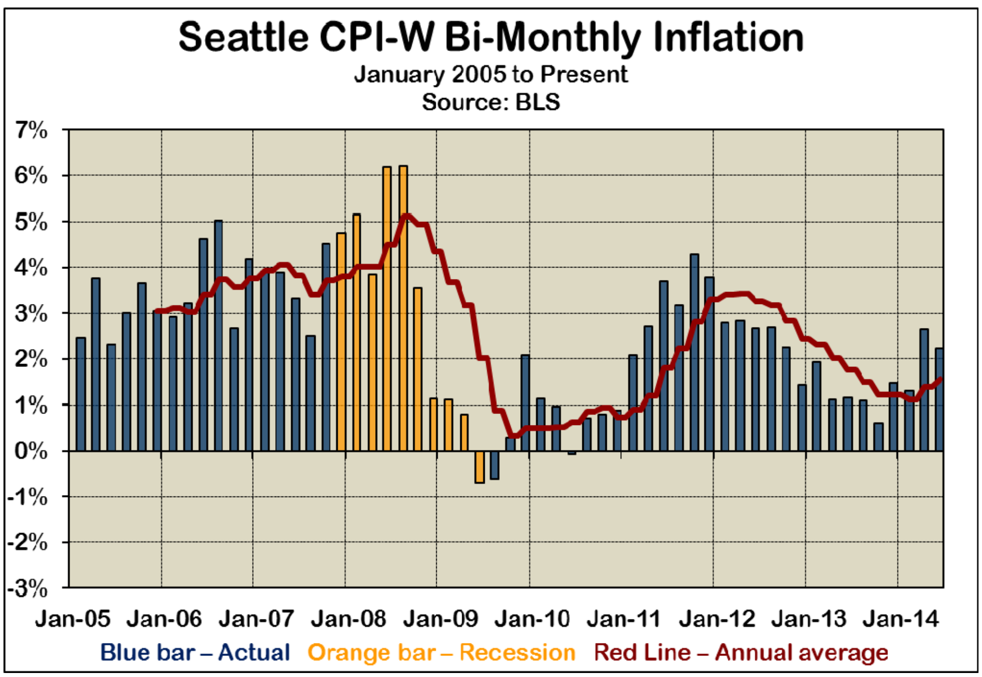
Other county economic indicators are showing improvement too. Housing prices began falling in 2006 and fell significantly before beginning to grow again in early 2012. Since that time housing prices have been recovering quickly although the pace has begun to slow in 2014. The Seattle Case-Shiller home price index, pictured below, shows the change in residential prices over time. The June 2014 value is 6.3% higher than June 2013.



Building permit activity in King County has also been strong for several years which continues to indicate growth in construction of single and multi-family structures. The following chart indicates the value of permit activity in King County.



As noted previously, local inflation is a key driver of county expenditure levels because some county labor contracts include adjustments for the cost-of-living that are related to local inflation values and because price increases affect the cost of county purchases, such as service contracts, health care, leases, food, gas, technology equipment, and vehicles. Annual inflation in the Seattle area has been modest but has accelerated in 2014 compared to 2013 levels.



In general, economic forecasts for King County indicate that the local economy will continue to improve with significant employment and personal income growth, strong taxable sales growth and modest inflation. The discussion below provides more information on the economic forecasts.

2. The Cost of King County Government

King County's Comprehensive Financial Management Policies have been designed to "provide a common language and policy framework for King County finance professionals and decision makers," guide fiscal stewardship of the County while "remaining responsive to the needs of county residents and the changing regional economy."[1] These policies mandate that King County's Office of Performance, Strategy and Budget undertake efforts:

> *To help the County benchmark and compare service delivery against other jurisdictions and identify efficiency opportunities, the County will create measurements for the cost of government and update those measurements for each biennial budget. Such measurements are intended to be broad in nature, such as: total revenues per capita per year, the number of County FTEs per person in the County, and the total expenditures of the County compared to the total income in the County. The analysis should also measure the cost of government in the County's unincorporated and incorporated areas.*[2]

This research laid the initial groundwork to gain a broader understanding of how costs to provide County services change over time, compared to variations in communitywide economic indicators which result from fluctuations in the economy. Evaluating these trends can enable decision-makers to gauge and effectively utilize local public feedback in budget and policy development. The project reviews a 10-year period from 2004 to 2013.

In order to establish King County's "cost of government," selected economic and financial indicators were evaluated in preparation for future benchmarking work against other jurisdictions of similar size and demographics, normalized by the governments' functions:

Indicator 1 – Revenues per Capita
Indicator 2 – Tax Revenues
Indicator 3 – Expenditures per Capita
Indicator 4 – Expenditures by Function (per Capita)
Indicator 5 – Total Full-time Equivalent (FTE) Employees per Capita
Indicator 6 – Personal Income per Capita
Indicator 7 – Property Tax Revenues per Capita
Indicator 8 – Assessed Full Value (Property values)

Indicators 1-6 and 8 were selected and evaluated according to the methodologies outlined in the ICMA's *Evaluating Financial Condition: A Handbook for Local Government.*[3] Sources for all King County's revenues, expenditures, employees, and assessed full value (property value) figures were gathered from King County's Comprehensive Annual Financial Reports (CAFRs)[4] from 2008 and 2013. King County's demographic, inflation, and income figures were gathered from the U.S. Census Bureau, U.S. Bureau of Labor Statistics and the U.S. Bureau of Economic Analysis, respectively. All dollar figures are represented in constant dollars, adjusted for inflation using a 2003-based Seattle-Tacoma-Bremerton CPI-W (calculated by ICMA methodology).

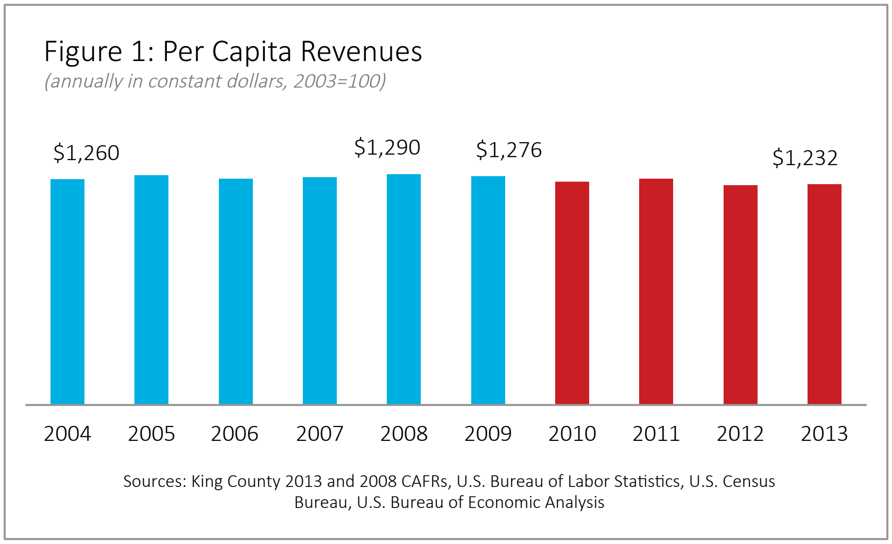
Indicator 1 – Revenues per Capita (Fig.1)

$$\frac{\text{Net operating revenues (constant dollars)}}{\text{Population}}$$

Total revenues generated per capita declined on average by 0.9% per year since 2009 as a result of the financial crisis from 2007 and 2008 which impacted King County's general government operations; total revenues per

[1] King County Office of Performance, Strategy and Budget, "Comprehensive Financial Management Policies" (King County, 2014), Page 2.
[2] Ibid, Page 5 (Point #6 under subtitle of Key Budget Features)
[3] Groves, Sanford M., Godsey Valente, Maureen, and Karl Nollenberger. Evaluating Financial Condition: A Handbook for Local Government. Washington, D.C.: International City/County Management Association (ICMA), 2003. Print.
[4] King County. Finance and Business Operations Division. Comprehensive Annual Financial Report. Seattle: FBOD, 2008 and 2013. Print.

capita in 2013 were still below 2008 levels. In comparison, total revenues per capita grew on average by 1.2% annually between 2004 and 2007, when there was stronger economic performance. Overall, revenue growth per capita has been generally flat with an average annual growth rate of 0.2% in this last decade.

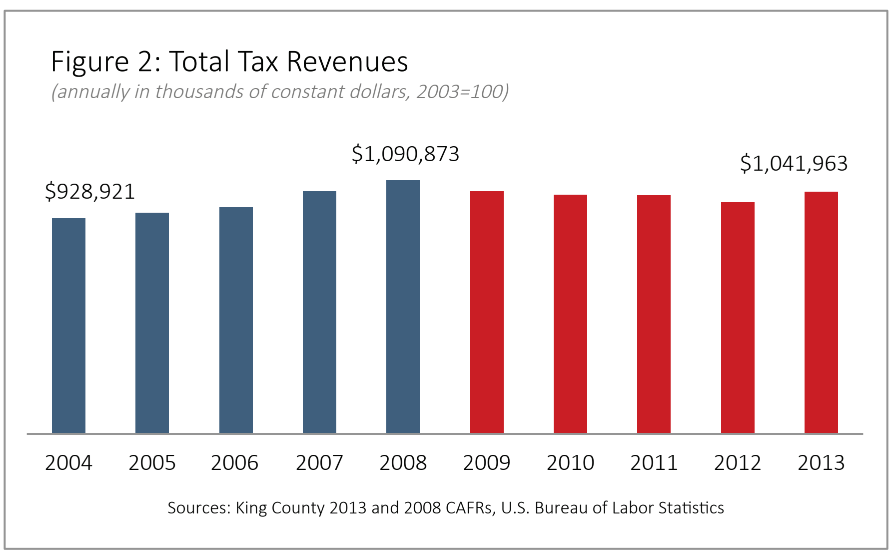


Indicator 2 – Tax Revenues (Fig. 2)

Tax revenues (constant dollars)*

Following the 2008 economic downturn, the County's tax revenues generally stagnated with an average annual growth rate of -0.9% between 2009 and 2013. In comparison, tax revenues from 2004 through 2008 grew annually at an average rate of 4.6%. In the last decade, annual tax revenues have fluctuated dramatically from one year to the next (e.g. tax revenues in 2007 grew by approximately 7% from the previous year, and declined by over 4% from 2008 to 2009). By 2013, these revenues had not reached the County's 2008 levels of total tax revenues.

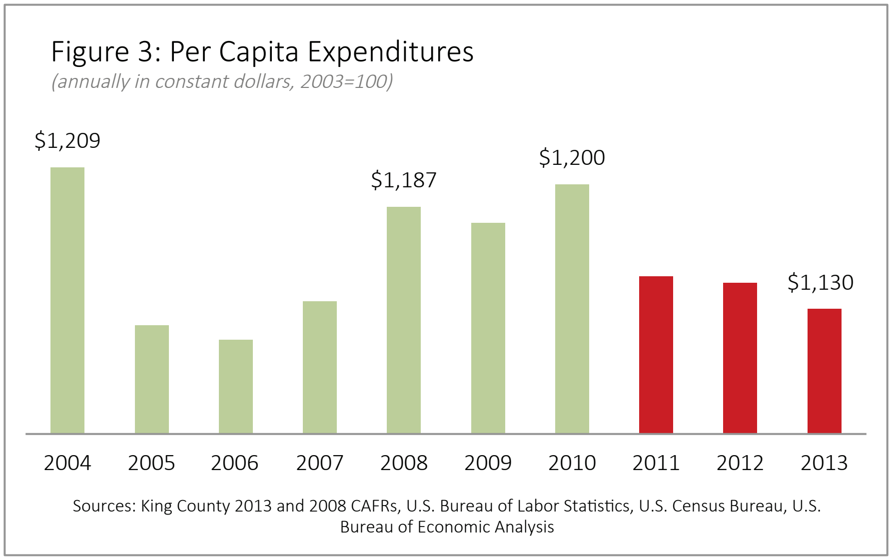
*Tax revenues are defined as property taxes, retail sales and use taxes, business and other taxes, and penalties and interest on delinquent taxes.



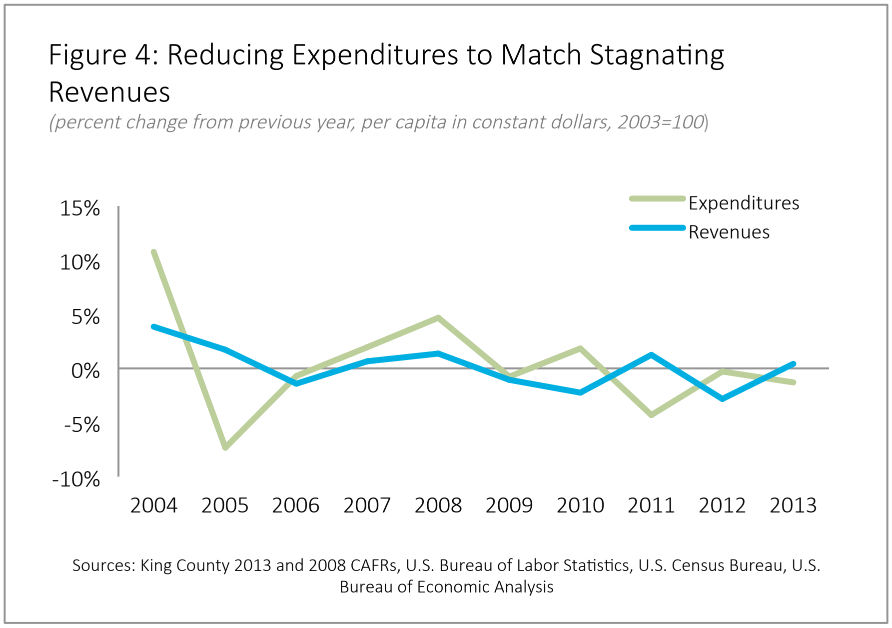
Indicator 3: Expenditures per Capita (Figs. 3 and 4)

$$\frac{\text{Net operating expenditures (constant dollars)}}{\text{Population}}$$

King County's expenditures increased on average by 1.5% per year from 2005-2010. However, in 2010 the County implemented efficiency measures and budget reductions that cut services across county functions, and reduced annual expenditure growth by about 2%.



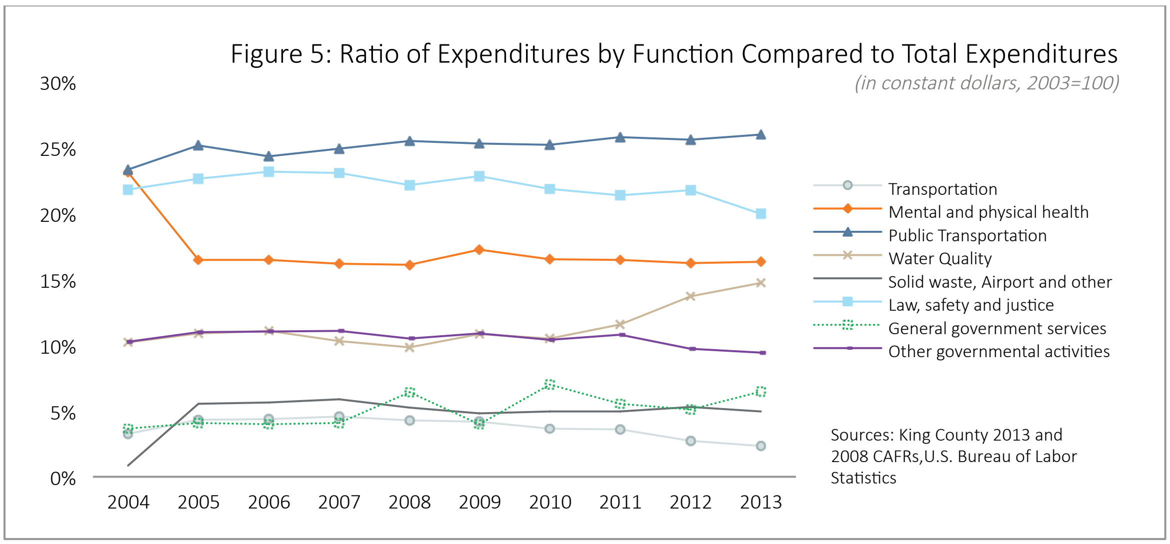
Rates of growth for total revenues and expenditures per capita have both slowed; revenues remained flat in the last decade, while expenditures have been cut to align with stagnating revenues (Fig.4).



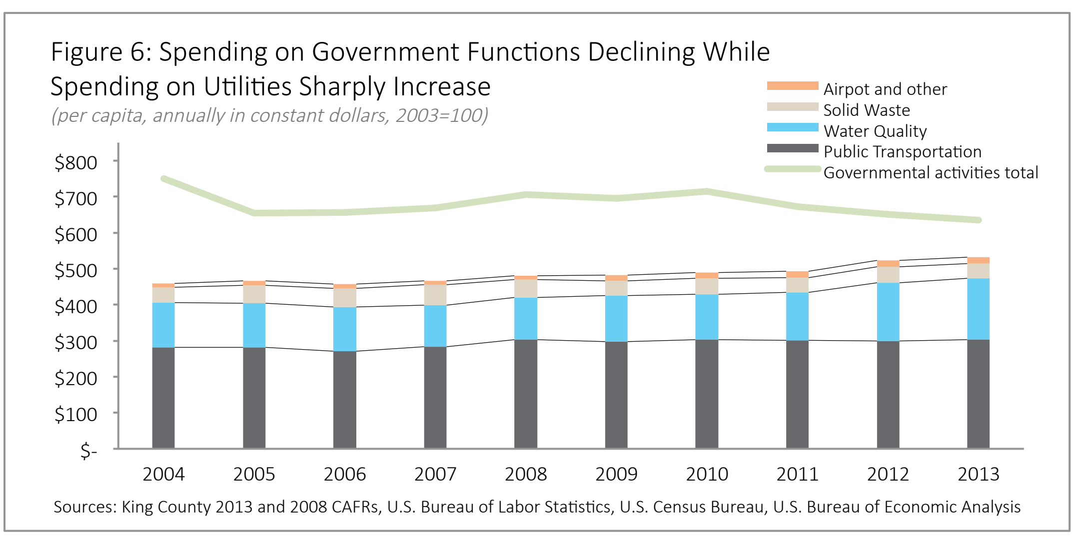
Indicator 4 – Expenditures by Function per Capita (Figs. 5 and 6)

$$\frac{\text{Operating expenditures for one function}}{\text{Total net operating expenditures}} \quad \& \quad \frac{\text{Operating expenditures for one function}}{\text{Population}}$$

From 2009 to 2013, tax-funded spending for basic government services (governmental activities[5]) declined annually on average by 2.4% (Fig.5), whereas spending on fee-supported business functions – airports, public transportation, solid waste and wastewater treatment – grew on average by 2.8% per year. The largest declines by function occurred in law, society and justice, and mental and physical health sectors, both of which declined on average by about 1% per year from 2009 to 2013. (Operating expenditures were adjusted for inflation.)



Similarly, per capita spending on primary government functions (see footnote 5) has been steadily declining since 2010 on average by 3.9% per year. Public transportation spending per capita has stagnated since 2008, while per capita spending on Water Quality (wastewater) has increased annually on average by 10.8% since 2010. Much of the growth in the wastewater spending is attributable to the 2011 implementation of the Brightwater Treatment Plant.

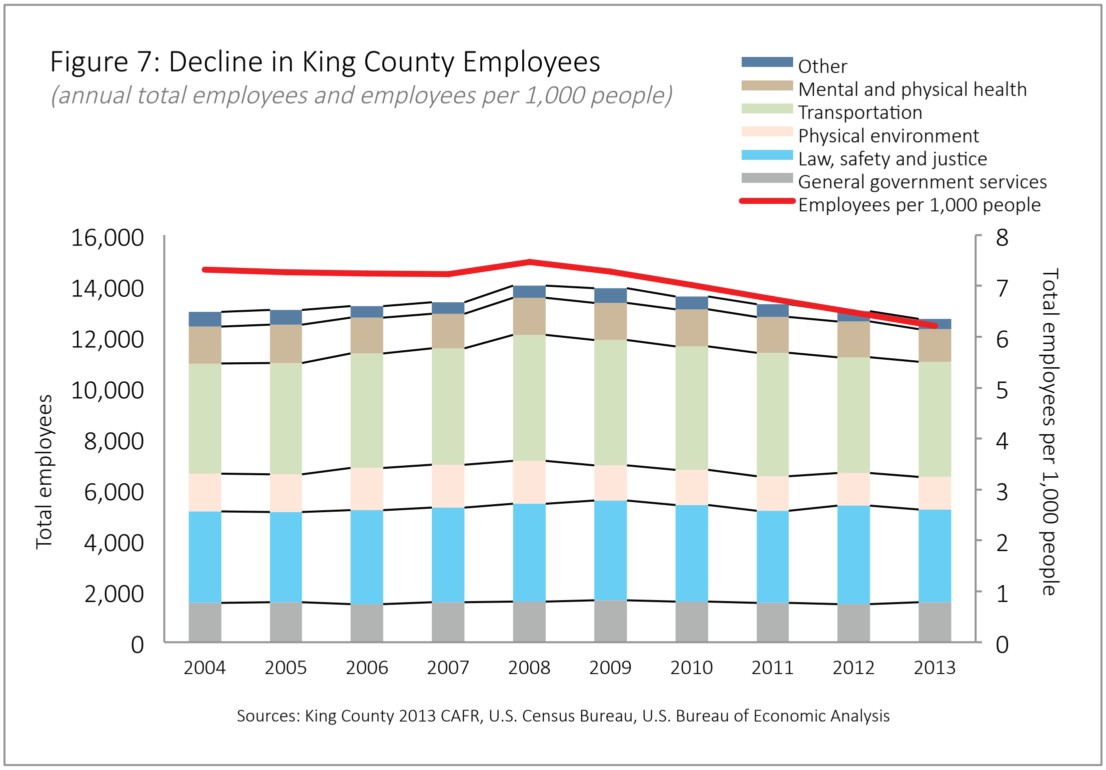


[5] Governmental activities: general government services; law, safety and justice; physical environment; transportation (roads); economic environment; mental and physical health; culture and recreation; and interest/debt service. In Figure 5, "other governmental activities" include economic environment, physical environment, culture and recreation, and interest/debt service.

Indicator 5: Total Full-time Equivalent (FTE) Employees and Total FTEs per Capita (Fig. 7)

$$\frac{\text{Number of municipal employees}}{\text{Population}}$$

Total FTEs countywide have decreased dramatically since 2008, especially in sectors of law, safety and justice, mental health and physical health, and public transportation; the County had about 14,000 total FTEs in 2008 compared to nearly 12,700 employees in 2013.



Employees per 1,000 people	2008	2009	2010	2011	2012	2013
	7.47	7.28	7.01	6.74	6.47	6.21

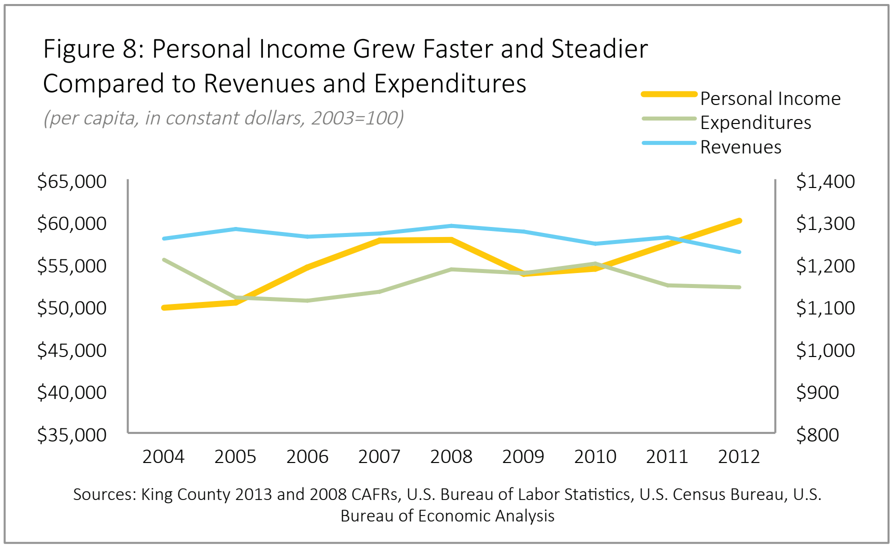
On average, between 2009 and 2013 the sector of law, safety and justice fared slightly better – with number of employees decreasing at a rate of 1% – compared to transportation, which lost employees at a rate of 1.7% per year. County contracting with suburban cities contributed to a portion of the increase in total employees for law, safety and justice between 2011 and 2013, as deputies were added to the County's payroll under contract obligations.

Additionally, from 2008 to 2013 annual King County employees per capita (expressed in "per 1,000 people") have steadily declined – from 7.47 employees to 6.21 employees – paralleling the trend of expenditures by function for basic government functions (Fig. 6, refer to footnote 5 for list of functions). Some of this decrease in employees per capita since 2008 has been driven by the annual average population growth of about 1%.

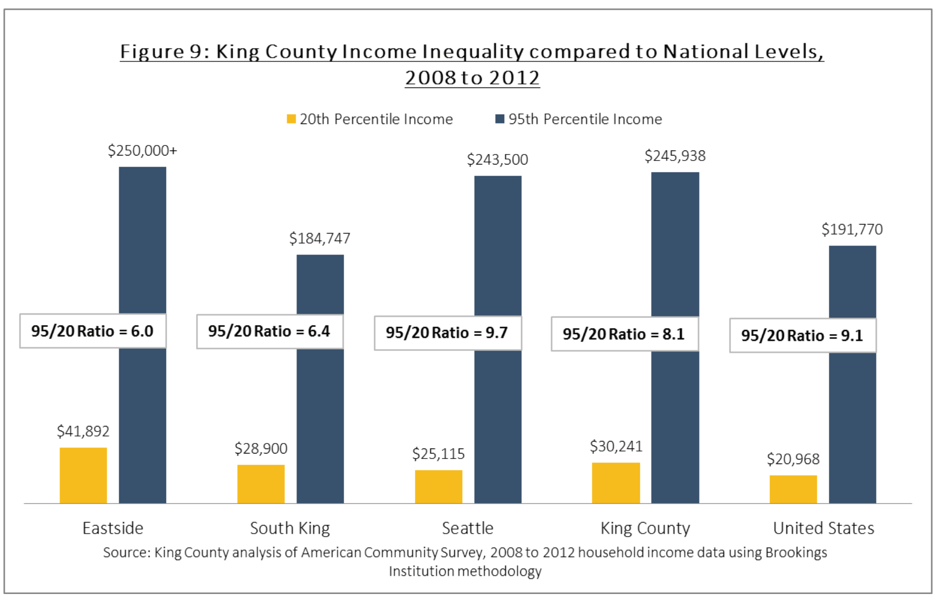
Indicator 6 – Personal Income per Capita (Fig. 8 and Fig.9)

$$\frac{\text{Personal Income (constant dollars)}^{*}}{\text{Population}}$$

King County's aggregate personal income represents the County's total economic resources. From 2004 to 2012 personal income per capita (Fig. 8) grew at a faster annual rate – on average by 3.1% – and more steadily compared to the more volatile growth rates of per capita revenues and expenditures (Fig. 4).



While personal income per capita continued to grow steadily after 2008 (Fig.8), so did income inequality between the poorest and most affluent households across King County. The "95/20 ratio" (Fig.9) is an economic indicator which "represents the distance between a household that just cracks the top 5 percent by income, and one that just falls into the bottom 20 percent."[6,7] Income inequality of King County within Seattle city limits was higher



6 Berube, A. (2014). All Cities Are Not Created Unequal. Retrieved from http://www.brookings.edu/research/papers/2014/02/cities-unequal-berube

7 The Brookings Institution methodology was applied by Office of Performance, Strategy and Budget, to generate "95/20" ratios for King County using American Community Survey data. School districts in Census tract data were used to represent geographic differences: Bellevue and Lk. Washington = Eastside, Federal Way and Kent = South King County and Seattle = City of Seattle. These values may understate the degree of inequity in the Eastside due to confidentiality and data limitation.

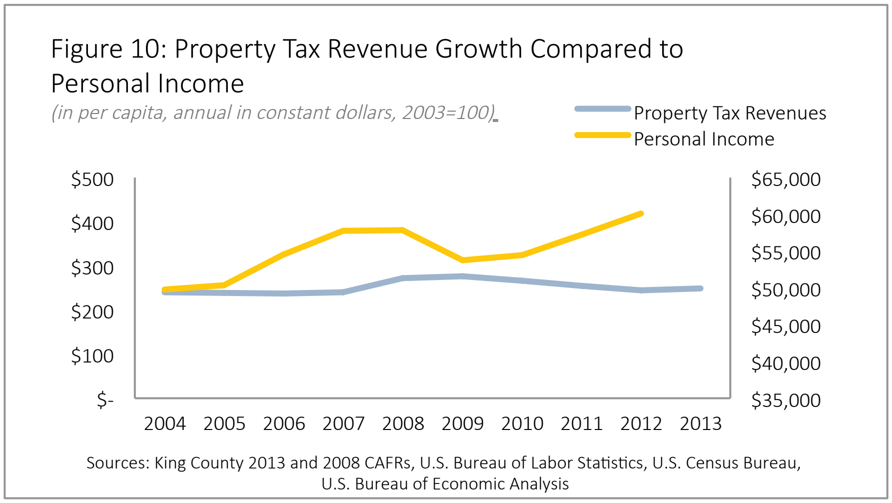
*Latest aggregate personal income data is available only through 2012.

compared to national levels, whereas King County as a whole fared slightly better. It is important to note that the degree of inequity in household incomes may be understated for Eastside and South King County due to limitations in U.S. Census data.

Indicator 7 – Property Tax Revenues per Capita (Fig. 10)

$$\frac{\text{Property tax revenues (constant dollars)}}{\text{Population}}$$

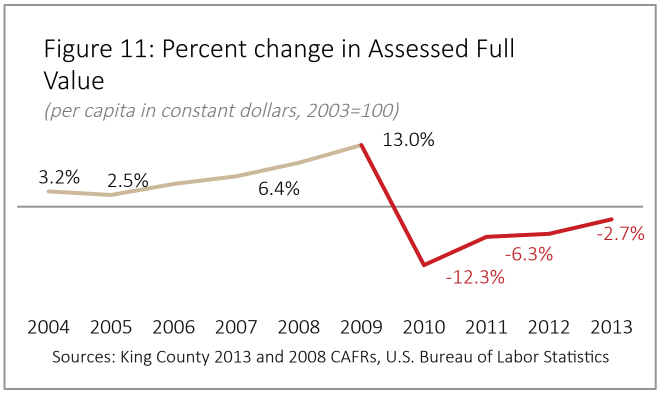
Per capita property tax revenues grew annually at an average rate of about 1.2% from 2004 to 2013, at less than half the growth rate of personal income per capita, which increased steadily on average by about 3.1% per year (Fig. 10). The sharp increase in property tax revenues from 2007 to 2009 can be attributed to the real estate boom in the previous years (assessed property values lag actual market values). However, property taxes started to decline steadily in 2010 steadily due to the economic downturn. By 2011, per capita personal income reached pre-recession levels while per capita property tax revenues remained below the 2009 peak.

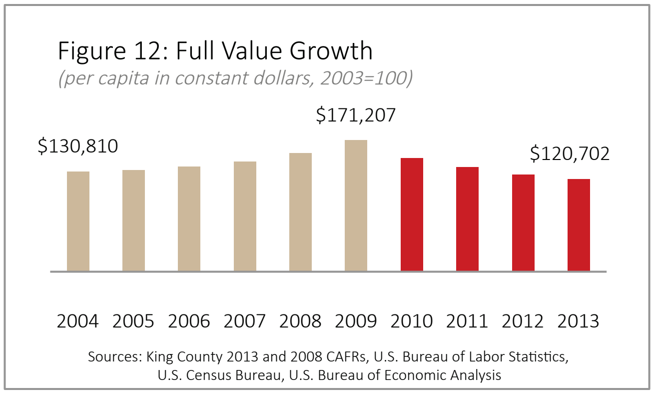


Indicator 8 - Assessed Full Value per Capita (Figs. 11 and 12)

$$\frac{\text{Change in property value (constant dollars)}}{\text{Property value in prior year (constant dollars)}}$$

Property tax collections are based on assessed full value (AFV) of properties. Property values depreciated considerably between 2009 and 2013 at average annual rate of nearly 6.8%. By 2013, growth rates in assessed full value had not recovered to 2004 levels and per capita property values still lagged substantially behind 2009 peak. Overall, per capita assessed full values in 2013 had not yet reached 2004 levels (Fig. 12).





3. **King County Revenue Forecasting**

The state of the national and local economy has a significant impact on many of the revenue sources within the County. The reduction in the wealth of U.S. households, high unemployment, and flat prices that characterized the 2007-2009 recession and extended into the recovery significantly reduced the amount of sales taxes collected by the County. The Real Estate Excise Tax (REET) collections were drastically reduced from the peak of the housing boom as both the prices and volume of sales shrunk. Annexations and years of falling assessed values in the unincorporated areas pushed the levy rate for the Unincorporated Areas Levy (Roads Levy) to its maximum rate resulting in significant reductions in the amount of property tax revenue the County received for road maintenance. However, most of the revenue streams have now begun to grow again and assessed value grew in 2014 for the first time since 2009.

In 2008, King County voters passed a charter amendment that changed how revenue forecasting for the King County budget is accomplished. The amendment required the County Council to establish a Forecast Council to adopt economic and revenue forecasts that must be the basis of the Executive's budget proposal and established a new agency called the Office of Economic and Financial Analysis (OEFA) to perform the forecasting work. The Forecast Council is made up of the Executive, two County Council members and a County employee with knowledge of budgeting and finance appointed by the Executive (currently the Director of the Office of Performance, Strategy and Budget). OEFA provides forecasts to the Forecast Council that are then reviewed and adopted. By policy, revenue forecasts are done at the 65th percentile confidence level to provide a degree of conservatism in the forecasts.

OEFA uses statistical models to forecast County-specific economic variables (e.g. property values and local inflation) and the major County tax revenue streams (e.g. sales taxes). In general, the models use local or national forecasts for variables like personal income, consumer prices and employment. The forecasts for these economic variables are sourced from three economic forecasting services and Washington's Economic and Revenue Forecast Council. The table below lists some of the inputs into the models.

Economic Assumption Summary

	2013	2014	2015	2016	2017
King County					
Nominal Personal Income (% chg, PSEF)	4.0%	4.7%	5.1%	5.2%	5.2%
Unemployment Rate (ratio, PSEF)	5.2%	5.0%	4.7%	4.7%	4.6%
Taxable Sales (% chg, PSEF)	7.1%	3.6%	5.6%	5.1%	5.0%
Housing Permits (% chg, PSEF)	3.9%	8.1%	9.3%	3.4%	-1.6%
Consumer Price Index - U (% chg, ERFC)*	1.2%	2.2%	2.1%	1.6%	1.8%
Construction Employment (% chg, PSEF)*	7.3%	4.2%	5.3%	3.9%	3.5%
Washington State					
Nominal Personal Income (% chg, ERFC)	3.2%	4.4%	5.2%	5.7%	5.7%
Unemployment Rate (ratio, ERFC)	7.0%	6.1%	5.8%	5.7%	5.7%
Multi-Family Permits (% chg, ERFC)	25.5%	3.8%	-10.9%	2.6%	-1.8%
United States					
Real GDP (% chg, GIB)	1.9%	1.7%	3.0%	3.3%	3.2%
Unemployment Rate (ratio, GIB)	7.4%	6.4%	6.0%	5.8%	5.6%
Ten-year Treasury Yield (level, GIB)	2.4%	2.7%	3.3%	3.7%	4.4%
Consumer Price Index (% chg, BCCF average)	1.5%	1.9%	2.1%	2.2%	2.3%
House Prices (% chg, ERFC)	9.5%	0.5%	-1.1%	-1.2%	-0.6%

* Puget Sound Region
GIB = Global Insight Baseline Forecast - July 2014
ERFC = Washington State Economic & Revenue Forecast Council - June 2014
PSEF = Puget Sound Economic Forecaster - June 2014
BCCF = Blue Chip Consensus Forecast - July, 2014

King County Revenues

Total County Revenues

King County projects total revenues of over $8.9 billion in 2015/2016[9], which King County distributes to more than eighty distinct operating and capital funds across the county government. The largest funds include those for transit, wastewater, public health, surface water management, roads and the General Fund. The largest revenue sources are taxes, intergovernmental revenues and charges for services. Together they account for over ninety percent of all revenues. Taxes include several major property tax levies, four different sales tax assessments, and taxes on real estate transactions. Intergovernmental revenues and charges for services include both direct contracts, interfund payments, and other services provided by the County.

Taxes account for an estimated thirty-two percent of the county's total operating revenues. The major tax sources for the County include property taxes, sales and use taxes, hotel and motel taxes, telephone excise taxes to support the enhanced-911 system and real estate excise taxes (REET). Total King County tax revenue is projected to be $2.8 billion in 2015/2016. These revenues support operating expenses, debt service, and some capital projects. Property taxes are the largest single tax source for the county, with a proposed countywide levy of approximately $635.1 million in 2015. This is made up of a regular levy of about $462.2 million, an EMS levy of about $116.7 million, and conservation futures, transit and bond redemption levies which total about $56.2 million.

Property Tax

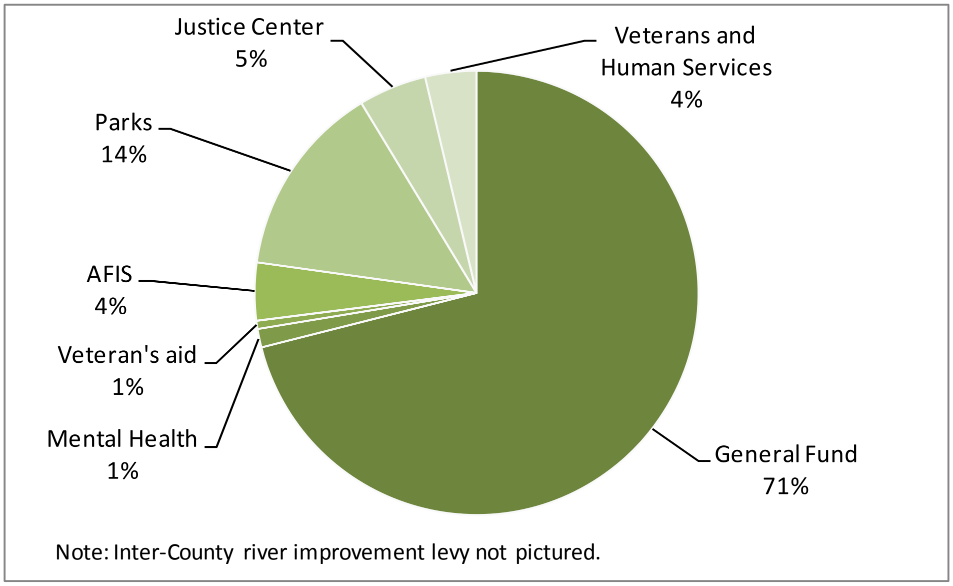
Property taxes are levied primarily on real property owned by individuals and businesses. Real property consists of land and permanent structures, such as houses, offices and other buildings. In addition, property tax is levied on business machinery and equipment. In accordance with the Washington State Constitution and state law, property taxes paid by a property owner are determined by a taxing district's rate applied to the value of a given property. In the County, the total property tax levy varies based on the make-up of the various taxing districts including fire districts, school districts, other special purpose districts, cities, and the countywide levy. The King County assessor determines the fair market value of properties, which is intended to generally reflect 100 percent of the property's market value.

In 2014, the total countywide regular levy rate was $1.33 per $1,000 of assessed value. This includes the undesignated general fund and the dedicated millage for mental health/developmental disabilities programs, veterans' aid, inter-county river improvements, and voter approved lid lifts. For an owner with a $350,000 home value, the total countywide tax liability for the regular levy was $466 in 2014.

The following chart illustrates the various components of the County's 2014 regular levy: the non-voted general purpose levy, and the four voter approved levies known as lid lifts (the voters authorized taxation above the statutory "lid" or limit). The 2015 property tax rates cannot be known with certainty until final assessed values are available in late 2014.

[9] Interfund transfers, overhead rates and other transactions are duplicates in some funds in the total revenue figure.

2014 Countywide Regular Levy



The regular levy is only one part of the total property tax bill due from County residents. Property taxes are collected through the regular levy, additional countywide levies for transportation, conservation futures and bond redemption, the unincorporated areas levy, the emergency medical services levy and others. The following funds all receive property tax collections in King County:

- General Fund
- Mental Health
- Veteran's Service
- Inter-County River Improvement
- Automated Fingerprint Identification System (AFIS)
- Parks
- Children and Family Justice Center
- Veterans and Human Services Levy
- Emergency Medical Services (EMS)
- Conservation Futures
- Unincorporated Areas/Roads
- Transit
- Unlimited General Obligation Bond Redemption

The annual growth in property tax revenue is restricted by state law in two ways. First, the state limits growth in the amount of tax revenue a jurisdiction can collect to one percent increase on the previous base each year plus the taxes assessed on the value of new construction. Beginning in 1973, state law limited the annual growth of the County's regular levy (i.e. general purpose plus voted lid lifts) to 6 percent. In 2001, Washington voters approved Initiative 747 (I-747) which changed the 6 percent limit to the rule noted above. In November 2007, I-747 was found to be unconstitutional by the State Supreme Court. However, the governor and state legislature in a special session reenacted Initiative 747 with House Bill 2416, and it was adopted in late 2007.

The property tax rate is also limited by State statute; the total levy for the County, cities and junior taxing districts is capped at $5.90 per $1,000 of assessed value (AV). This includes limiting the countywide levy to $1.80 per $1,000 of AV, and the unincorporated areas levy to an additional $2.25 per $1,000 of AV.

Over the past few years, the assessed value of property in the unincorporated area has declined and the unincorporated levy has reached its statutory limit. The combination of levy limits, the reduction in assessed values, and annexations has reduced County Roads Fund property tax collections in recent years from $86.1 million in 2011 to $67.5 million in 2013. For 2015, the levy is expected to increase to approximately $78.9 million, as assessed value has begun to grow.

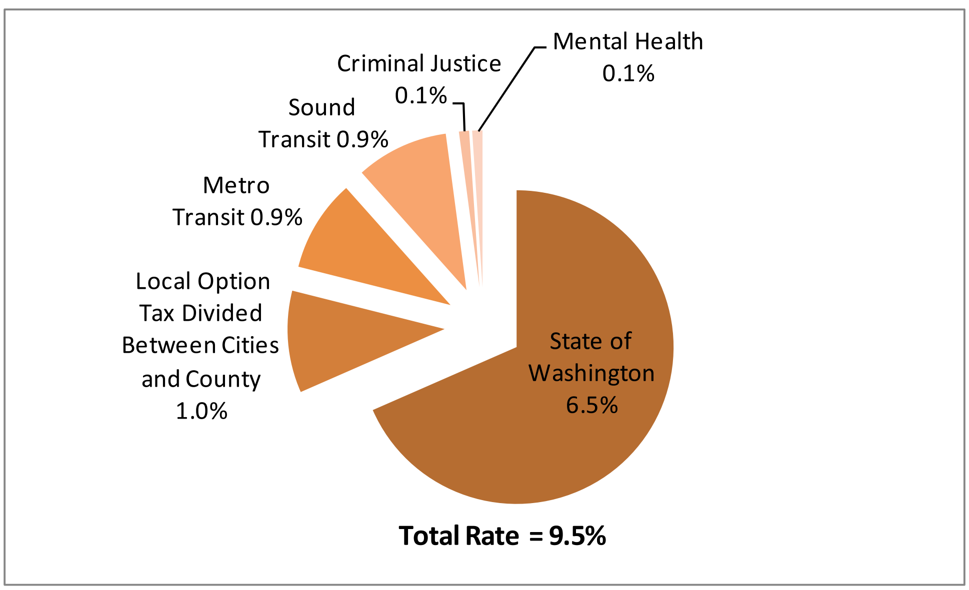
As mentioned previously, the overall countywide property tax collection for County budgeted funds is projected to be $635.1 million in 2015 up from $627.4 million in 2014. This amount includes an enhanced parks' levy that voters approved in August 2013 that initially levies about $63.6 million in 2014 and lasts for six years (2014-2019). The countywide levy also includes the Automated Fingerprint Identification System (AFIS) lid lift (effective 2013-2018), the Veterans and Human Services Levy (effective 2012-2017) and the Children and Family Justice Center Lid Lift (effective 2013-2021). Voters also approved the EMS levy in November 2013 which will be effective 2014-2019.

Retail Sales Tax

The retail sales and use tax (sales tax) is imposed on the sale of most goods and certain services in the County. The tax is collected from consumers by businesses that, in turn, remit the tax to the state. The state provides the County with its share of these revenues on a monthly basis. The sales tax rate is 9.5% for most taxable transactions.

The basic sales tax rate is a composite of separate rates for several jurisdictions. The county's portion is 1 percent of sales in the unincorporated area and 0.15 percent of the sales in the incorporated areas. The County receives sales tax beyond the basic rate to support transit, criminal justice and mental health programs. The following chart indicates the distribution of sales taxes for locations in the county with a tax rate of 9.5%.

2015 Sales and Use Tax Rates in King County



The sales tax is primarily affected by changes in the economy and by the geographic areas from which it is collected. The county's public transportation, mental health, and criminal justice programs receive revenues from countywide retail sales, with unincorporated areas constituting less than four percent of the tax base.

The following funds receive sales tax collections in King County:

- General Fund
- Transit
- Mental Illness and Drug Dependency

Legislative changes have also impacted sales tax collections for King County. In 2008, Washington State entered into the Streamlined Sales Tax agreement and began implementation in July 2008. Previously, the sales tax was based on the jurisdiction from which the product was shipped, with that jurisdiction receiving its local option sales tax. Under sales tax streamlining, the destination of the product determines the jurisdiction that receives the local portion of the sales tax. Because this negatively impacted some jurisdictions, the State is providing mitigation payments to some jurisdictions including King County. This increases sales tax revenues relative to what they would have been without mitigation.

Contract Revenue

Contracts are a significant source of funds for several agencies. By contracting with the County, cities are able to take advantage of the County's economies of scale, as well as the expertise and experience of its workforce. Examples of contract revenues are the Sheriff's provision of deputies to cities and transit agencies, District Court contracts and regional animal services. These contract revenues are further explained in the individual agency sections. General Fund contract revenues are forecast to be $178.8 million in the 2015/2016 biennium.

Revenue from Other Entities

The County receives revenue from federal, state and local governments. These revenues include capital and operating grants for various programs and liquor board profits which come from license fees charged to distributors and retailers under the state's privatized liquor sales program developed in response to the passage of Initiative 1183 in November 2011.

Licenses and Permits

The County requires individuals and companies conducting business in unincorporated King County to obtain a business license. Some business activities require additional licenses referred to as professional and occupational licenses. The County also assesses fees for public-safety purposes (e.g. pet ownership) and charges a variety of fees for the use of public facilities and rights-of-way.

REET

King County levies the Real Estate Excise Tax (REET) in unincorporated King County and administers state and city REET taxes throughout the County. REET consists of two 0.25 percent taxes on real estate transactions. REET revenues were high during the peak years of the housing boom (2005-2006) at over $11 million each in each year but fell drastically during the recession and during the recovery. Recently, collections have begun to recover and each is forecasted at just under $5.7 million in 2014 rising to $5.9 million in 2015 and $5.6M in 2016. REET collections are adversely impacted by annexations.

4. Summary of the General Fund Financial Plan

This section provides a synopsis of the General Fund financial plan including revenue and expenditure trends, reserves, and a General Fund outlook. The revenues and expenditures for General Fund programs are further described in the specific budget book chapters. Consistent with the comprehensive financial management policies, longer range projections are shown in the fund financial plans. For additional detail, consult the financial plan on the following page as well as the footnotes detailing the underlying policies and assumptions.

Revenues

Since 2008, General Fund sales tax collections have declined to a low in 2010 and have since started to increase. Current forecasts expect sales tax revenues to rebound to 2007 levels in 2014. Property tax continues to slowly but steadily increase, due to new construction, recent increases in assessed value, and because the County's regular tax rate is still far below the legal limit. Contract and interfund revenues are expected to remain stable in the next biennium and charges for services for King County Sherriff's Office (KCSO) operations in the unincorporated area will increase in 2015 to reflect the service provided. Interest earnings remain low. Federal and State funding is expected to be flat in the future and is an area of future risk. It is also important to note that some fines, penalty and forfeits do not increase with inflation and in some instances have declining volumes; this has an overall negative impact on General Fund revenues.

Beginning in 2015, sales taxes that used to be deposited into the Children and Family Services Fund will be deposited directly in the General Fund. There will also be an offsetting General Fund Transfer to Human Services so the impact of this technical change is net zero. In addition, the Parking Facilities Operating Fund has been added to the General Fund as a subfund. This additional level of transparency will increase overall revenue and expenditures, but has a bottom line net zero impact to the financial plan.

Total General Fund revenues are expected to grow by 4.6% in 2017/2018 and 5.4% in 2019/2020. These are biennial growth rates.

Expenditures

For 2015/2016, General Fund expenditures are forecast to be approximately $1.48 billion. This represents a year-over-year growth rate of 1.9% from estimated levels. Expenditure growth has fallen due to cost reducing efficiencies, program reductions, internal service rebates, and through the use of fund balance to support capital expenditures in the 2015/2016 proposed budget.

In addition to providing ongoing funding for criminal justice and general government services, The General Fund provides support for non-general fund programs through a series of transfers. The total General Fund transfer amounts for 2015/2016 are listed below. More details on these transfers can be found in the corresponding sections of the budget book.

- Department of Community and Human Services: $14,370,000
- Public Health: $58,815,000
- Regional Animal Services: $5,262,000
- Department of Permitting and Environmental Review: $4,184,000
- King County Department of Information Technology Capital: $1,490,000
- Facilities Management Division Capital: $10,000,000
- Facilities Management Division Operating: $396,000
- Water and Land Resources Division: $1,700,000
- Limited Tax General Obligation Debt Service: $45,500,000

Total General Fund expenditures are expected to grow by 6.4% in 2017/2018 and 6.2% in 2019/2020. These are biennial growth rates.

Reserves and Fund Balance

The 2015/2016 Executive Proposed budget results in an ending fund balance of $74.9 million in 2016. This is $10.2 million higher than current projections for ending fund balance in 2014. The 2015/2016 Proposed Budget maintains the undesignated fund balance at 6.5 percent which is in line with County policies and financial practices of other AAA bond rated governments.

The 2015/2016 Proposed Budget includes adjustments to existing reserves and creates new reserves for specific capital projects, landslide mapping, and South Park Bridge operations. The Risk Reserve is increased to reflect additional revenue and expenditure uncertainty. The reserve for Emergent Needs is not proposed for 2015/2016.

Further information on designations and reserves can be found in the financial plan notes in this section.

Financial Outlook

The General Fund is managed to achieve the following goals: maintain current services at the appropriate quality and quantity, maintain a target undesignated fund balance of 6.5% and maintain the highest bond ratings. This is an ongoing challenge since expenditure growth is projected to exceed revenue growth in the upcoming biennium and beyond. The largest component of the General Fund revenue, property tax, is capped at 1 percent growth plus new construction per year. The largest component of expenditure growth, labor costs, is driven by inflation and increases in benefits and retirement costs. All of these annual cost increases exceed the property tax growth rate. The long term growth rate assumptions for expenditures exceed the revenue growth rate by just over 1% per biennium. However, additional unavoidable costs typically surface during each budget cycle which exacerbates the budget imbalance.

It is important to recognize that the long term financial outlook of the General Fund has improved over the past six years primarily as a result of bending the cost curve downward and improving budget practices. Efficiency efforts will continue in 2015 and 2016 in order to keep downward pressure on the expenditure cost curve.

Even with the past successes and continuing efforts, additional adjustments will be necessary to balance the General Fund budget. The anticipated 2017/2018 biennial gap is between $35 and $40 million. The gap is comprised of the ongoing structural imbalance, the continued ramp down of MIDD supplantation, and a higher level of funding for the Major Maintenance program.

In addition, the General Fund faces considerable risks and liabilities over the next ten years. The county has planned and created reserves for a number of these risks, but most are unfunded. Below is a partial list of the financial and operational risks that are being monitored.

- Natural disaster
- Mental Illness and Drug Dependency (MIDD) Supplantation ramp down
- Unfavorable labor contracts
- Economic downturn
- Central rate increases (i.e. facilities, information technology) due to contraction of other funds
- Ongoing pressure from other funds (Public Health, Roads,
- Increase in local inflation
- Diminishing returns on efficiencies

- Litigation
- Reduction in federal and state revenue
- Caseload fluctuations in the criminal justice system
- Loss of contract revenue from other jurisdictions
- Impact of deferred maintenance on county facilities
- Impact of Affordable Care Act (ACA) Excise Tax
- State pension rate increase
- Flexrate increase above 4%
- Claims spike (benefits, workers comp)
- Increase in unemployment, PERS1, legal costs
- Cyber attack
- IT system failure
- Communicable disease outbreak
- Landslides
- Eastside Rail Corridor (ERC) maintenance

It is important to note that while these risks have been identified, reserves do not exist in the 2015/2016 financial plan for all of these issues. As a matter of practice, it is not necessary to reserve for all of the potential risks. Certainly, some additional costs will be incurred as a result of the identified risks, but it is highly unlikely that all risks will be realized. The level of reserves in the General Fund is determined by balancing the available resources and the County's appetite for unfunded risk.

To help mitigate some of the risks highlighted above, the proposed General Fund budget maintains an ending undesignated fund balance of 6.5% of certain revenues, which is over the required 6% minimum. The Risk Mitigation reserve within the General Fund is approximately $32 million and the Rainy Day Reserve Fund remains over $20 million. The proposed General Fund financial plan is detailed on the following pages, along with supporting footnotes.

Summary of 2015/2016 General Fund (10) Financial Plan (in millions)

Summary includes Inmate Welfare and Garage Operations subfunds as reported in CAFR

	2013/2014 BTD [1]	2013/2014 Estimated [2]	2015/2016 Proposed	2017/2018 Projected	2019/2020 Projected
BEGINNING FUND BALANCE	**123.5**	**123.5**	**64.7**	**74.9**	**57.4**
REVENUES [3]					
Property Tax [4]	473.1	619.1	643.3	672.2	701.2
Sales Tax [5]	144.6	198.7	226.9	242.8	262.0
Intergovernmental Receipts	118.4	171.7	178.8	187.1	199.8
Interest Earnings and Pool Fees	3.3	3.4	4.0	4.1	4.2
Federal and State Revenue	29.9	40.8	42.8	42.8	42.8
Fines, Forfeits, Charges for Services, Other	160.7	214.4	211.1	215.9	226.4
Interfund Transfers	93.2	141.7	178.7	188.5	201.4
General Fund Revenues	**1023.2**	**1,389.8**	**1,485.6**	**1,553.3**	**1,637.8**
EXPENDITURES [6]					
Operating Expenditures	(1012.1)	(1,367.4)	(1,439.3)	(1,526.7)	(1,623.0)
CIP Expenditures [7]	(16.6)	(19.7)	(11.5)	(15.0)	(16.0)
Debt Service [8]	(41.7)	(46.3)	(45.5)	(50.1)	(51.5)
Supplementals/Carryover/Reappropriations	0.0	(24.8)	0.0	0.0	0.0
Potential Additional Costs [9]	0.0	(1.3)	0.0	0.0	0.0
Underexpenditures/Overcollections [10]	0.0	10.0	20.0	20.9	22.2
General Fund Expenditures	**(1070.3)**	**(1,449.5)**	**(1,476.3)**	**(1,570.9)**	**(1,668.3)**
Other Fund Transactions [11]	0.0	0.8	0.9	0.0	0.0
Ending Fund Balance	**76.4**	**64.7**	**74.9**	**57.4**	**26.9**
DESIGNATIONS AND SUBFUNDS [12]					
Designations [13]	(2.4)	(2.4)	(2.4)	(2.4)	(2.4)
Subfund Balances [13]	(4.6)	(4.6)	(2.4)	(1.8)	(1.2)
EXPENDITURE RESERVES					
Carryover and Reappropriation	(0.9)	(0.9)	0.0	0.0	0.0
Salary & Wage	0.0	0.0	0.0	0.0	0.0
CIP Capital Supplemental Reserve [14]	0.0	0.0	(0.7)	(0.7)	(0.7)
MIDD Buy-Back Reserve [15]	0.0	0.0	0.0	(11.4)	(22.8)
Executive Contingency	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
South Park Bridge Post Annexation Operations :	0.0	0.0	(0.5)	(1.5)	(2.5)
Strategic Innovation Plans [17]	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Emergent Needs	(3.1)	(3.1)	0.0	0.0	0.0
Landslide Mapping [18]	0.0	0.0	(0.1)	(0.1)	(0.1)
Planning Staff	(0.1)	(0.1)	0.0	0.0	0.0
Risk Reserve	(16.4)	(16.4)	(31.8)	(37.3)	(45.7)
Reserves	**(27.7)**	**(27.7)**	**(38.0)**	**(55.4)**	**(75.6)**
Ending Undesignated Fund Balance [19]	**48.7**	**37.0**	**36.9**	**2.0**	**(48.7)**
6% Undesignated Fund Balance Minimum	16.5	32.3	34.1	35.7	37.5
Over/(Under) 6% Minimum	31.3	4.7	2.8	(33.7)	(86.2)
Over/(Under) 6.5%	**30.0**	**2.0**	**0.0**	**(36.7)**	**(89.3)**
Rainy Day Reserve	20.1	20.1	20.2	20.3	20.4

2015/2016 Proposed General Fund Financial Plan Footnotes

[1] 2013/2014 BTD (Biennial To Date) reflects actuals collections from 1/1/2013 through 6/30/2014. Actual data based on EBS Report GL_010 and reconciled to CAFR.

[2] 2013/2014 estimated figures have been adjusted to reflect approved 2014 supplementals and updated revenue forecasts.

[3] Revenue estimates for 2017 - 2020 are based on forecasts adopted by the Forecast Council and revenue estimates provided by General Fund appropriation units. The percentages below are the expected percent change over the prior budget cycle. These are biennial growth rates.

	2015/2016	2017/2018	2019/2020
Property Tax	As Proposed	4.5%	4.3%
Sales Tax (including sales tax dedicated to criminal justice)	As Proposed	7.0%	7.9%
All Other	As Proposed	3.6%	5.0%
Blended Revenue Growth Rate		*4.6%*	*5.4%*

[4] Property Tax forecasts for 2015 - 2020 are based on August Office of Economic and Financial Analysis (OEFA) forecast adopted by the Forecast Council and assume the current property tax structure.

[5] Sales Tax forecasts for 2017 - 2020 are based on August Office of Economic and Financial Analysis (OEFA) forecast adopted by the Forecast Council and assume the current sales tax rate.

[6] Expenditure estimates for 2017/2018 and 2019/2020 are based on the following assumptions. The percentages indicate the expected percentage change over the previous budget cycle. The assumed flex rate percentage increase reflects current plan design and structure.

	2015/2016	2017/2018	2019/2020
CPI (Seattle July to June CPI W)	As Proposed	4.6%	4.8%
COLA & Step	As Proposed	6.2%	6.3%
Benefits	As Proposed	8.2%	8.2%
Retirement	As Proposed	10.3%	10.3%
Operating GF Transfers	As Proposed	6.7%	6.9%
Blended Expenditure Growth Rate		*6.4%*	*6.2%*

[7] CIP GF Transfers (in millions)

	2015/2016	2017/2018	2019/2020
Major Maintenance	8.0	10.0	10.5
Building Repair and Replacement	2.0	3.0	3.5
KCIT CIP	1.5	2.0	2.0
Total	11.5	15.0	16.0

[8] The debt service schedule for 2015 - 2020 is based on the following table:
(in millions)

Debt Service Elements	2015/2016	2017/2018	2019/2020
Existing Debt Issues	43.6	41.9	36.2
New Debt Issuance	0.6	7.2	14.2
Debt contingency for new issues and variable rate	1.3	1.0	1.0
Total Debt Service	45.5	50.1	51.4

Based on current projections, projected debt service expense will not exceed the County's 6% debt limit.

[9] Potential additional costs in 2013/2014 include expenditures related to labor settlements and year end requests.

[10] The 2015/2016 Proposed Budget includes vacancy assumptions in the majority of GF operating budgets. This is budgeted directly in appropriation units. An additional annual underexpenditure assumption of $10 million for all General Fund budgets is included. The underexpenditure is assumed to grow at the same rate as expenditures.

[11] Other fund transactions in 2013/2014 include an accounting adjustment in 2013 and a rebate from the Benefits Fund in 2014. In 2015/2016, approximately $0.9 million in District Court IT operating costs will be supported by either KCIT fund balance or through bond proceeds.

[12] Fund balance set aside in reserve is used to offset known future increases in costs, to mitigate known risks, or to fund specific programs in the future. Designations and subfund balances reflect fund balance associated with dedicated revenue streams. Ending undesignated fund balance is fund balance set aside for unknown financial and operation risks.

[13] Designations and subfund balances include the following for each of the years (in millions):

	2013/2014	**2015/2016**	**2017/2018**	**2019/2020**
Loans	(0.3)	(0.3)	(0.3)	(0.3)
Crime Victim Compensation Program	(0.1)	(0.1)	(0.1)	(0.1)
Drug Enforcement Program	(1.8)	(1.8)	(1.8)	(1.8)
Anti-Profiteering Program	(0.1)	(0.1)	(0.1)	(0.1)
Dispute Resolution	(0.2)	(0.2)	(0.2)	(0.2)
Real Property Title Insurance	(0.0)	(0.0)	(0.0)	(0.0)
Inmate Welfare Fund Balance	(4.2)	(1.9)	(1.9)	(1.9)
Ex-CJ Fund Balance	(0.4)	(0.4)	(0.4)	(0.4)
Total	(7.0)	(4.8)	(4.8)	(4.8)

[14] This reserve sets aside fund balance for specific capital projects in 2015/2016. These projects would be part of a 2015/2016 supplemental proposal. The specific projects include DC Shoreline Access Control, Kent Animal Shelter Security Upgrade, and the Archives and Record Center Planning.

[15] The Mental Illness and Drug Dependency (MIDD) Buy Back Reserve is intended to support the criminal justice programs currently funded by the MIDD fund through supplantation legislation authorized by the state. Supplantation ramp down begins in 2015 and continues into 2017/2018. Fund balance is set aside to support these ongoing programs.

[16] The reserve is intended to support King County's portion of ongoing operational costs of the South Park Bridge. These costs are assumed to begin in 2016 after the annexation of the North Highline Sliver and Triangle. The operating costs are currently in the Roads budget.

[17] This reserve supports funding for areas that the Council and Executive identify for Strategic Innovation Priority (SIP) Plans.

[18] This reserve provides matching support for future Landslide mapping grants.

[19] County policy requires undesignated fund balance of 6%-8% of certain revenues. The 2015/2016 proposed budget sets the undesignated fund balance at 6.5%.