

INTRODUCTION

After growing rapidly for four years, King County's economy slowed dramatically during 2001. Employment growth in the County slowed from its torrid pace of the 1990s, and employment soared, doubling from 3.4 percent in December 2000 to 6.8 percent in January 2002.

The 2002 outlook for King County and the nation is cloudy. The terrorist strike of September 11, 2001 was quickly followed by the stock market's near record breaking drop on September 17 and by Boeing's announcement of up to 30,000 layoffs. National events have quickly pushed an already struggling local economy into recession. Economists are generally uniform in expecting little to growth for the first half of 2002, followed by a recovery in the second half of the year. Monetary policy has been very aggressive during 2001 taking interest rates to a forty-year low. This budget document contains forecasts that were, for the most part, developed prior to the terrorist attack and Boeing's announcement, with revision and adjustments made during October and November. Given the volatile state of the economy, the budget office anticipates further revisions throughout 2002.

During 2001, the traditional revenue sources for King County went from very rapid growth to actual decline. Sales tax growth on a monthly basis slowed from rates over 13% to -6% by the second quarter of 2001. Numbers in the second half of the year were also negative, although December, fueled by low interest rates, was little changed from the previous year. Low interest rates, however, also mean lower returns on county fund balances.

While property taxes are generally unaffected by economic changes, passage of Initiative 747 in November capped property tax revenue (net of new construction) at one percent starting with 2002 property tax collections. Altogether, revenue was reduced by

The following information provides more detail on our general economic forecast, a description of each of the King County revenue sources and a fund by fund analysis. The forecasts are conservative but realistic and intended to provide a sound basis for funding decisions.

Table 1: Table Revenue Changes from Proposed to Adopted Budget

October/November Changes to Revenue Forecast	Amount (millions)
Property Taxes [Initiative 747]	-\$1.7
Sales Tax [Revised forecast]	-\$0.7
Investment Earnings [Revised forecast]	-\$0.6
Other changes [Fund transfers, fee increases, revised forecasts]	\$2.1
Net impact	-\$0.9

General Forecast

The forecast was developed by surveying local economists, reviewing published State and national forecasts, and tracking recent economic developments. This review was conducted to identify the economic trends expected for 2002-2004 and to make forecasts of selected indicators that would be consistent with the local outlook. As in the past, the Budget Office relies on the regional forecast

ECONOMIC AND REVENUE FORECAST

prepared by Conway Pedersen Economics for the general economic outlook as well as separate King County forecasts prepared by these same economists.

The rapid growth of the 1990s is forecast to give way to a period of slow to slightly negative growth in the remainder of 2001 and 2002. Not since the early 1980s has the economy been this weak. Most economic indicators are forecast to experience almost no growth, and some indicators project negative growth for 2002. However, the national economy is expected to accelerate during the latter part of 2002 due to several factors:

- Repeated rate reductions by the Federal Reserve Bank are likely to stimulate the economy
- Inventories are at low levels and should be rebuilt during the year
- Fiscal policy will stimulate the national economy

Consumer spending has been the driving force of the national economy during the economic expansion of the 1990s. This appears to be changing as consumers have holstered their wallets. Automobile sales declined in July 2001 by over 9% from the prior year, and the annual rate is now 7% lower than just five months ago. Similarly, consumer spending on other durable goods, such as furniture and building materials has fallen. Consumer confidence has fallen since its peak in 1997, although it remains above the recessionary levels of the early 1990s.

Locally, employment here hasn't declined, but growth is slowing. Prior to Boeing's announcement, layoffs at aircraft and parts manufacturers (dominated primarily by Boeing) have declined from over 1,500 per month to nothing by early 2001. Regionwide aerospace employment peaked at 108,600 in July 1998 and it bottomed in January 2001 at 82,600, to recover slightly to 83,900 by July 2001. Offsetting the Boeing decline has been the very rapid expansion in business service. The "new economy" grew rapidly between 1999 and 2000 as nearly 15,000 jobs were added in business services, but then cooled rapidly in 2001 with only an additional 3,000 jobs added by July and a decline from late 2000 levels. Other sectors have similarly cooled: Construction employment, which was growing every quickly, only grew by 2.6%.

The shakeout in the dot.coms is now nearly over. Employment declines at Amazon.com, Homegrocer.com, Onvia.com, Hardware.com, and others have taken some of the glamour off the dot.coms. Regionwide the employment impact is minor. Of more concern is the decline in Microsoft stock's value and stock option income. According to Conway Pederson Economics, the loss of Microsoft stock option income is likely to cost the region .4% of its employment.

The forecasted growth in employment and other variables for the Puget Sound regional (taken from the September 2001 *Economic Forecaster*) is presented in Table 1 below:

Table 2: Economic Forecast for Puget Sound Region

<i>Economic Forecaster, September 2001 Forecast, Puget Sound Region</i>				
	2000	2001	2002	2003
Annual Growth (% change)				
Employment	2.2	.9	-.3	1.4
Personal Income (Cur \$)	5.1	2.2	3.2	5.4
Consumer Price Index	3.7	3.5	2.1	2.5
Housing Permits	-3.6	-3.7	-11.0	-4.7
Population	1.3	1.2	1.3	1.2
Taxable Retail Sales	7.6	.8	.1	3.6
Unemployment Rate	4.1	4.9	5.8	5.7

There is much uncertainty involved in looking towards 2002. Among the factors are:

- What will the impact be on the economy from the terrorist attack of September 11, 2001? Will consumer's rein in their spending and stall the economy? Will government and private spending spur the economy into growth?
- How many jobs will be eliminated at Boeing and for how long?
- Will the fallout in the telecommunications sector affect other technology firms in the region?
- Will the Japanese economy recover from its doldrums?
- Will Washington's agricultural and forestry economies recover and provide additional growth to the region's ports?

Consumer Spending and Personal Income

Consumers have been the driving force for the economy. But the outlook for consumer spending is precarious as the economy slows; uncertainty spreads from the terrorist attack on New York City, and other cautionary news. Signs of slowing consumer spending are evident as automobile production declines and sales of other durable goods have declined.

The *Economic Forecaster* predicts that consumption will slow in the Puget Sound region in 2001 and 2002. Personal income has already fallen and employment growth in many of the fast growing sectors has evaporated. Personal income will fall even more with layoffs eminent.

The largest consumer-sensitive revenue source is sales tax. King County uses sales tax revenues for transit, criminal justice, and the General Fund¹. The forecasted slowdown will lead to a reduction in the rapid growth of sales tax from nearly 20% in the fourth quarter of 1999 to an actual decline in sales tax revenues in 2001 and a decline in 2002. Adjusting for inflation, sales tax growth will be negative in both 2001 and 2002, an experience not seen in this region since the recession of the early 1990s. In the next decade, Conway Pederson Economics forecasts retail sales will grow between 4.6 and 5.4% annually.

Interest Rates and Interest Earnings

Interest earnings continue to be difficult to forecast. During 2001, CX interest earnings were somewhat above forecast both because of somewhat higher balances and because long-term holdings in the portfolio held up the investment rate. However, late in 2001 the interest rate has fallen dramatically and 2002 and beyond will be affected by the current low rate environment. Because of the volatility in interest earnings, which are attributable to both changes in the fund balances and changes in interest rates, the Budget Office continues to provide a conservative interest earnings forecast.

For 2002, it is predicted that there will be one further reduction in the interest rate by the Federal Reserve with the potential for increases later in 2002. Interest rates have been forecast using the futures prices on the New York and London markets and correlating them with historical pool earnings rate. However, the fiscal markets have been extremely skittish since the terrorist attack and it is very difficult to predict pool investment earnings.

¹ The General Fund includes the Current Expense subfund, Diverted Road Taxes subfund, Refund Levy Taxes subfund, Designated for Contingencies subfund, Children and Family Services subfund, and the Inmate Welfare subfund.

KING COUNTY REVENUES

Total revenues to the County exceed \$2 billion dollars, which King County distributes into over 50 separate funds. The largest funds include those for transit, wastewater, surface water management, roads, and the County general fund. Table 2 identifies the major revenue sources for King County for all funds.

Table 3 Major Revenue Sources

	1999 Adopted	2000 Adopted	2001 Adopted	2002 Adopted
Taxes	765,481,815	719,275,061	715,108,733	746,596,328
Licenses & Permits	16,040,636	18,022,369	18,066,214	18,472,802
Intergovernmental Revenue	26,756,947	26,756,947	26,756,947	35,829,205
Federal Grants-Direct	26,852,073	28,650,976	30,207,497	32,359,967
Federal Shared Revenues	732,617	678,590	688,182	699,091
Federal Grants-Indirect	47,740,164	44,605,870	62,580,257	65,173,089
State Grants	81,737,617	99,941,683	103,615,392	100,044,636
State Shared Revenues	177,911	176,000	1,301,000	1,045,016
State Entitlements	26,326,768	46,590,108	53,726,160	30,125,795
Grants From Local Units	300,732	1,448,525	1,435,851	4,087,240
Intergovernmental Payment	118,425,668	123,027,845	135,928,603	124,894,603
Charges For Services	599,020,549	661,206,645	741,870,293	811,142,004
Fines & Forfeits	6,493,323	7,069,093	7,232,871	7,537,213
Miscellaneous Revenue				
Stadium Operating Revenues	6,853,074	221,000	0	0
Other Financing Sources	234,402,425	232,674,995	206,715,841	203,132,834
Subtotal Operating & Debt Service	1,957,342,319	2,010,345,707	2,105,233,841	2,181,139,823
Capital Project Revenues				
TOTAL COUNTY REVENUES	1,957,342,319	2,010,345,707	2,105,233,841	2,181,139,823

The largest revenue sources are taxes and charges for services. Taxes include property tax, sales tax, and taxes on real estate transactions. Charges for services include both direct contracts, interfund payments, and other services provided by the County.

In the remainder of this section, each of the major revenue sources is discussed. Following that will be a discussion of the County's funds, with a discussion of the Public Transportation and Water Quality Funds as well as the Current Expense Fund. An appendix provides further detailed information on revenues.

The following table presents our forecast short-term interest rates to be earned on County investment balances:

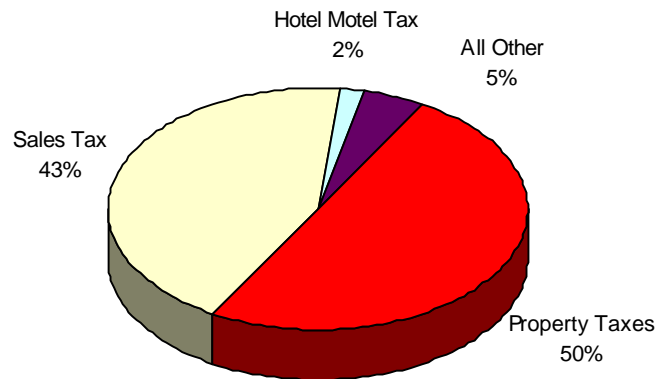
Table 4: Pool Earnings Rate Forecast

<u>2001 3rd Qtr.</u>	<u>2001 4th Qtr.</u>	<u>2002 Annual Average</u>
5.2%	4.6%	4.5%

Tax Sources

Taxes are the largest source of revenues to King County, accounting for 31.9% of all operating revenues and 62% of the revenues to the Current Expense Fund. The major tax sources for the County include property taxes, sales and use taxes, hotel and motel taxes, E-911 excise taxes, and other sources. Total King County tax revenues are projected to be \$752 million in 2002, an increase of 5.2% over the projected 2001 collections. These revenues support operating expenses and debt service. The property tax is the single largest tax source for the County, with a proposed levy of \$356 million in 2002, with an additional \$50 million collected for Emergency Medical Services (EMS). Figure 1 below provides the breakdown of the tax sources to the County.

**Figure 1:
Tax Sources to King County
All Funds, 2002 Adopted
\$755 Million**



PROPERTY TAXES

Property taxes are collected through the countywide levy, the unincorporated area levy, the Emergency Medical Services levy, and voter approved debt. These monies are dedicated to various funds within King County.

Property tax revenues are limited by both policy and State law. The levy amount is limited by the 101% annual lid on increases. The one important exception to this rule is that the value of any new construction is assessed at the prior year's levy rate and added to the proposed percentage increase to set the total new levy amount. Therefore, the level and value of new construction activity is the key variable in estimating the total revenues that the County can expect to receive from property taxes. Due to the limitations on property tax, the revenue source is a fairly stable source of income to King County.

The All-County Levy² is projected to go up by 3.8% in 2002, with new construction providing 2.8% of that increase; the base levy amount is proposed to increase by 1.0%, as required by Initiative 747. New construction assessments added to the tax rolls for 2002 of over \$4 billion reflected the previously strong local economy and were above the 2001 level of over \$3.8 billion. The overall All-County Levy is projected to increase from \$240 million to \$250 million in 2002. The amount remaining for

² The All-County Levy includes the CX fund and transfer to mental health/developmental disabilities, river improvement fund, human services, veterans' aid, Intercounty river improvement, and limited bond redemption.

ECONOMIC AND REVENUE FORECAST

the CX is this amount less debt service, AFIS, river improvement, and other designations. The CX revenues from the property tax levy are \$217 million or \$15.7 million more than the prior year³.

The Unincorporated Area Levy (traditionally called the "road levy") will levy nearly \$55 million in 2001, and will total \$54.2 million after distributions to new cities and undercollection.

SALES TAX

Among revenue sources to King County, the sales tax is that most affected by the economic slowdown in King County.

The Countywide sales tax rate is 8.8%. Of this amount, the following percentages are collected:

- 1.00% in unincorporated portions of the County
- 0.15% in incorporated portions of the County
- 0.80% transit tax after April 1, 2001
- 0.10% criminal justice tax (entire County)

Sales tax revenues are distributed to several funds within the County. The largest recipient is the Transit Fund. The following funds are projected to receive the indicated amounts in 2002:

- Public Transportation Fund receives \$240 million
- General Fund receives \$69.8 million
- Criminal Justice Fund receives \$11 million

The Criminal Justice Fund receives sales tax from the extra 1/10 of 1% Countywide tax approved by the voters in 1992. The total collected in the County is distributed to local jurisdictions (including unincorporated King County) on the basis of population after 10% is taken off the top and allocated to King County government. King County's total allocation will amount to approximately \$11.5 million from the sales tax in 2002.

The Transit Fund receives a Countywide sales tax which was set at a rate of 0.8% by the election of April 2001. The projected revenues for 2002 are \$240 million.

The sales tax is strongly influenced by changes in the economy and by the geographic areas from which it is collected. The Public Transportation Fund and the Criminal Justice Fund receive revenues from Countywide sales, while the CX Fund receives 1% from unincorporated area transactions and 0.15% from incorporated areas.

Total projected 2002 sales tax revenue to the General Fund is \$69.1 million, which includes the impact of annexations and incorporations. The 2002 tax receipts are projected to decline over the 2001 receipts by 2%. This estimate is consistent with the estimates developed by Conway and Associates for the Department of Transportation. Of the total, nearly \$3.2 million will be deposited to the Children and Family Services Subfund and \$3.57 million to the Sales Tax Reserve Subfund, with the remaining \$62.5 million dedicated to the Current Expense Subfund. These three subfunds comprise the General Fund.

³ This is before adjustment for the collection rate.

REAL ESTATE TAXES

King County levies the Real Estate Excise Tax (REET) in unincorporated King County and collects a 1% collection fee on all REET taxes collected in the County. High levels of real estate sales in 1999 - 2000 brought in significant amounts for all REET-related accounts. Because of the projected local recession, real estate related revenues will decline in 2002 and beyond. Housing sales are estimated to decline between 11 and 20%, and because the housing market is so volatile, a decline in sales of 20% has been assumed. Prices are projected to remain relatively constant or grow at about the local rate of inflation.

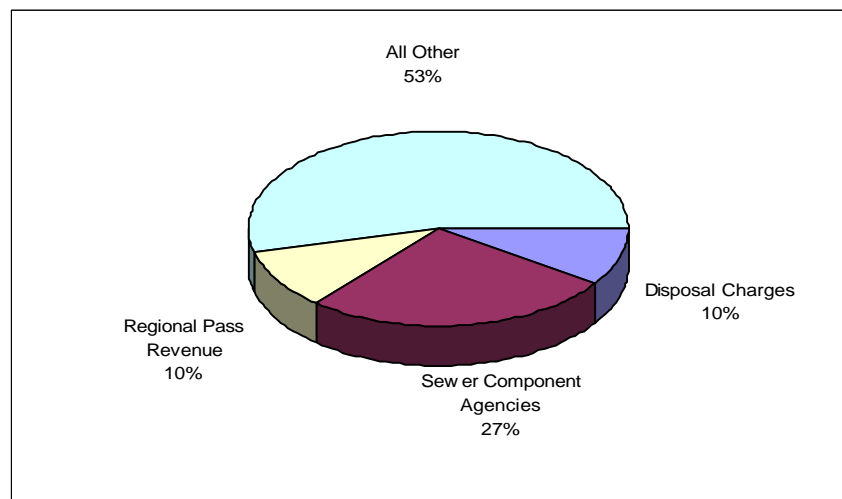
REET #1 and REET #2, both at 0.25%, are dedicated to the unincorporated area. Revenues from each tax are estimated at approximately \$6 million for 2001, declining to less than \$5 million in 2002. The REET collection fee, which is dedicated to the Current Expense Subfund, is also forecast to remain at about the same level as projected 2001 revenues of \$2.5 million.

Charges for Services

After taxes, the second largest income category is charges for services. Charges for services include wastewater contracts, transit services, public safety and court contracts, motor vehicle licensing, recreation programs, health services, recording and reproducing County documents, as well as other services. Charges for services also include interfund charges since many of these charges are not charges to the public, but charges to other County agencies. Charges for services provide the major source of revenue for the wastewater, transit, and solid waste funds. Figure 2 below provides the breakdown for charges for services.

As Figure 2 demonstrates, the majority of charges are associated with the disposal of solid waste, sewer treatment, and transit activities. The category of "All Other" includes primarily interfund charges within King County (such as personnel benefits) and many of these charges are not direct charges to other governments or to the public.

**Figure 2: Charges for Service Revenue
2002 Proposed - Total \$807 Million**



Other Revenues

Other revenues include revenues, which are primarily related to interfund payments. Some of the larger revenues include motor pool rental, insurance, facilities management, and related internal transfers.

FUND ANALYSIS

The County allocates its financial resources into a variety of accounting entities called "funds" or "subfunds" to account for revenues and expenditures. The use of multiple funds is necessary to ensure compliance with State budget and accounting rules, and to promote accountability for specific projects or activities.

Operating expenditures for services typically associated with the County, such as adult and juvenile detention, public safety, parks, and other functions, are accounted for in the General Fund. The Current Expense Fund is a subfund of the General Fund.

Many departments or programs have separate funds or subfunds. Special revenue funds include the Mental Health Fund, the Public Health Fund, Community Development Block Grants, Department of Development and Environmental Services, and other funds. Enterprise funds include Transportation, Wastewater, Solid Waste, and other functions. Capital project funds account for all resources received and used for the acquisition or development of capital improvement. Table 4 identifies the major funds and the revenues for each fund: Because of the large number of County funds, only three will be discussed here. Additional detail is provided in other sections of the budget document.

Public Transportation Enterprise Fund

The Public Transportation Fund is one of the largest funds operating within King County. This fund accounts for the operations and maintenance of public transportation facilities in King County. Primary revenue sources include sales taxes and passenger service fees. This discussion does not include the capital funds associated with public transportation. The total operating revenues received by the fund for 2002 are projected to be \$360 million. The local sales tax provides \$240 million, while passenger fees provide nearly another \$110 million.

Water Quality Enterprise Fund

Two funds account for the activities of the Water Quality Enterprise Fund. Fund 461 accounts for the operations and maintenance while fund 461-6 accounts for capital improvements and expansion of the County's water pollution control facilities under the King County Water Pollution Control Division. Two major treatment plants exist: the West Point Treatment Plant in Seattle and the East division Reclamation Plant in Renton. Major construction projects are funded through revenue bonds.

The Wastewater Treatment Division operating budget for 2002 is \$214 million and the capital budget is an additional \$103 million. The sources of funds for these are primarily customer charges (\$215 million) and bond proceeds (\$103 million), respectively.

Current Expense Fund Revenues

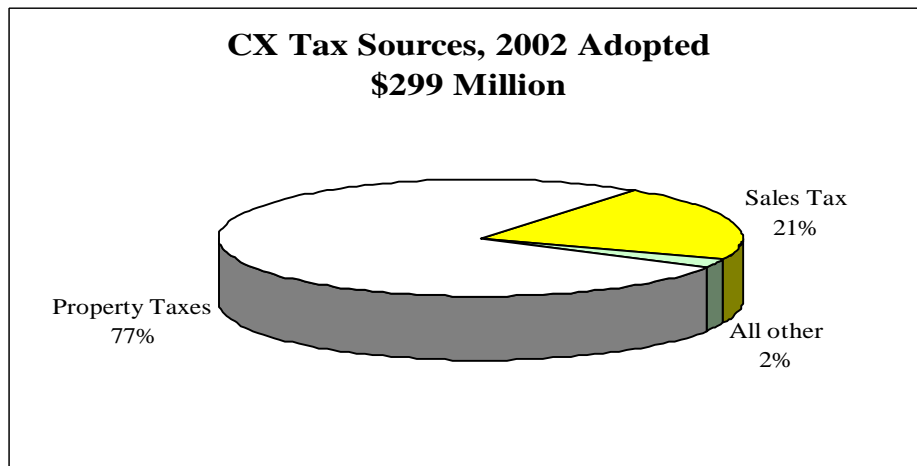
The Current Expense Fund (CX) raises its money from six principal sources. Table 5 indicates that the majority of this money is from taxes, which account for 60.5% of revenue sources.

Table 5

	1999 Adopted	2000 Adopted	2001 Adopted	2002 Adopted
Taxes	243,205,844	269,023,158	286,051,603	299,769,176
Licenses & Permits	5,159,300	4,886,200	5,140,510	5,569,001
Federal Grants-Direct	567,654	1,879,779	1,897,000	954,000
Federal Shared Revenues	38,000	39,140	39,140	40,314
Federal Grants-Indirect	4,293,999	4,328,755	5,900,152	4,817,776
State Grants	1,624,236	1,637,478	1,535,680	1,712,365
State Shared Revenues	141,000	176,000	176,000	181,280
State Entitlements	1,317,000	1,297,505	1,554,125	1,383,967
Grants From Local Units	70,728	14,000	14,000	2,614,420
Intergovernmental Payment	46,388,515	52,656,427	55,772,028	56,333,723
Charges For Services	57,621,784	76,991,057	80,258,079	82,090,013
Fines & Forfeits	6,223,771	6,810,093	7,164,871	7,524,713
Miscellaneous Revenue	17,851,879	15,454,140	19,219,214	15,842,712
Other Financing Sources	15,948,844	10,204,034	5,509,316	3,921,966
TOTAL REVENUES	400,452,554	445,397,766	470,231,718	482,755,426

Of tax sources, property tax is the most important. Figure 3 provides the breakdown of the tax sources:

Figure 3



CURRENT EXPENSE FUND CHARGES FOR SERVICE REVENUE

The greatest amount of change in revenues has occurred in the areas of charges for service and intergovernmental payments. Charges for services in the Current Expense Fund have grown rapidly in the past decade. In 1991, charges for services plus intergovernmental services accounted for \$64.7 million in revenue, or 24% of General Fund revenues. By 2002, this is projected to increase to \$138 million, or 24%. Table 5 provides detailed information for the past three years:

Table 6:

**CHARGES FOR SERVICE AND INTERGOVERNMENTAL
PAYMENTS REVENUE SUMMARY**

	2000 Adopted	2001 Adopted	2002 Adopted
Public Safety	32,916,218	34,972,055	36,938,290
Parks and Recreation	4,858,781	4,840,836	4,894,857
Resource Lands/Open Space	1,569,262	1,361,595	-
Licensing	8,966,840	9,409,300	8,978,205
Property Services	1,474,305	1,312,906	1,287,525
Records and Elections	7,329,943	9,098,139	9,314,512
Prosecuting Attorney	6,937,051	7,042,765	7,713,887
Superior Court	1,388,268	1,716,400	1,913,977
District Court	4,119,264	5,169,653	8,078,205
Judicial Administration	4,235,894	4,381,653	4,419,936
Adult Detention	27,913,529	25,630,559	25,861,230
Public Defense	2,811,908	3,982,612	2,274,437
All Other	25,126,221	27,111,634	27,697,844
Total	129,647,484	136,030,107	139,372,905

The largest two areas where the County provides contract services are Public Safety and Adult and Juvenile Detention. The King County Sheriff's Office provides contract services to many jurisdictions around the region, while the Department of Adult and Juvenile Detention provides contract services for the incarceration of misdemeanants.

Outyear CX revenue projection: In the year beyond 2002, the local economy should continue its long-term trend of slowing growth. Employment growth is projected to slow from 2% in 2003 to 1.3% by 2011. By 2011, the *Economic Forecaster* predicts that the region will have 2.1 million jobs, \$214 billion in personal income, and 3.7 million people.

CONCLUSION

King County's 2002 economic outlook projects a slowdown from the rapid growth of the past few years. There is significant uncertainty about the revenue outlook for 2002 and beyond. Given the terrorist attack, Boeing layoffs, and the stock market slump, it's fairly difficult to predict the economic outlook. Consumer spending has been driving the economy and it will determine much of what occurs in the next year.

[Link to Current Expense Financial Plan, 8 KB .pdf](#)

[Link to Current Expense Financial Plan Footnotes, 13 KB .pdf](#)

**Property Tax Levies by Fund
2001 and 2002**

	2001		2002	
Assessed Valuation				
All County	\$187,181,000,747		\$200,900,000,000	
Unincorporated Only	\$29,495,903,547		\$31,809,491,537	
All County Levy		Rate		Rate
Current Expense	\$201,665,414	1.0774	\$219,056,262	1.0904
Human Services	\$4,282,555	0.0229	\$4,464,431	0.0222
Veterans Aid	\$1,927,150	0.0103	\$2,008,994	0.0100
River Improvement	\$2,278,122	0.0122	\$2,374,872	0.0118
InterCounty River Improvement	\$50,000	0.0003	\$50,000	0.0002
Bond Redemption - Limited	\$19,181,000	0.1025	\$13,493,382	0.0672
Subtotal	\$229,384,242	1.2255	\$241,447,942	1.2018
Unincorporated Area Levy				
Road Services	\$50,936,973	1.727	\$54,932,347	1.727
Total Statutory Levy				
Bond Redemption -- Unlimited	\$38,499,728	0.2057	\$39,500,000	0.1966
EMS Levy -- All County	\$46,121,999	0.2464	\$50,225,000	0.2500
Farmlands Conservation Tax	\$11,698,812	0.0625	\$12,556,250	0.0625
Automated Fingerprint System	\$10,826,549	0.0578	\$9,855,604	0.0491
Regional Justice Center				
Total Property Tax Levies	\$387,468,303		\$408,517,143	

Note: Amounts in table represent levied amounts, not amounts which are collected.
Estimated collections are used in the adopted budget.