

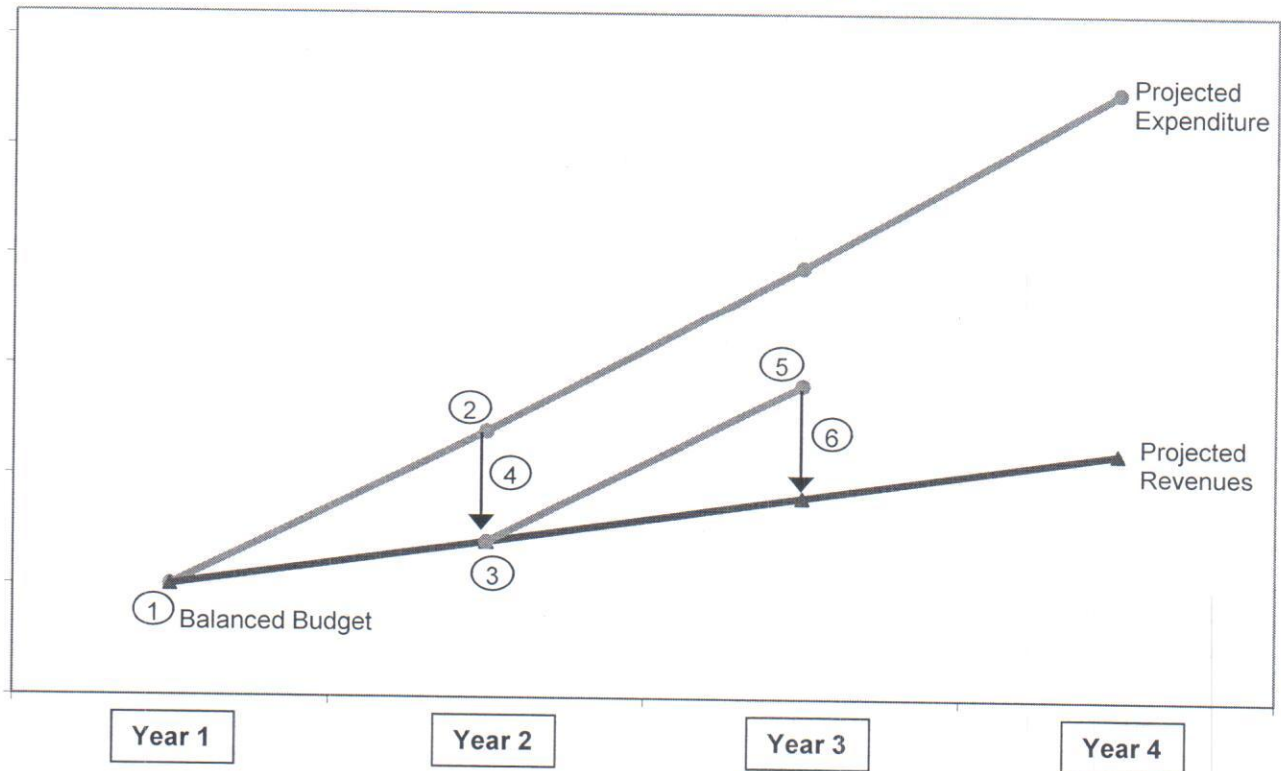
King County's budget shortfall

Structural gap explained

The discretionary portion of the King County budget is the General Fund (12% of the total budget) that pays for the traditional functions of county government, such as the Sheriff's office, and critical daily services not supported by other revenues. The budget crisis in the General Fund is a **structural** problem. The word "structural" is used to indicate that the crisis is a long-term problem caused by the structure of General Fund's revenues and expenditures. It is not a short-term problem caused by the downturn in the economy, although the size of the budget cuts required is exacerbated by that and other factors.

The structural gap is very simply that general fund revenues grow at a slower rate than expenditures. In years without a recession, general fund revenues grow at about 1 to 2 percent annually, while expenditures grow at 4 to 5 percent. In years with a recession, the structural gap is worsened by a decrease in revenue. The graph below illustrates the problem.

Illustration of structural gap



This graph shows projected expenditures growing at 4-5% and projected revenues growing at 1-2%.

- ① Budget is at balance in Year 1 with expenditures equal to revenues.
- ② With expenditures growing at 4-5%, the cost of offering the same programs in Year 2 grows to here.
- ③ Meanwhile, revenues grow at only 1-2%, to here in Year 2.
- ④ The difference between expenditure and revenue growth leads to a gap, requiring a cut in expenditures to balance the budget.
- ⑤ If the budget cut affects only the level, but not the growth of expenditures, remaining expenditures will continue to grow at 4-5%. The level of expenditures needed to provide the same level of services as in the previous year grows to here.
- ⑥ This structural difference in revenue and expenditure growth creates the need for another budget cut in the following year (Year 4). The problem continues until structural changes can be made that equalize the growth rates of expenditures with revenues.

The result of the structural gap is that the County becomes unable to provide the same level of services as in the previous year, requiring continuous cuts in the level of essential services to residents.

Simply cutting the level of expenditures or finding new revenues does not solve the structural problem, unless these actions increase the long-term *growth* of revenues and reduce *growth* in expenditures.

It is important to note that the structural gap is not confined to King County. Counties across Washington State face this continuing challenge between expenditures that increase at a much higher percentage than the revenues the county can collect.

Other factors affecting the budget shortfall

Revenue

There are several factors that have led to or exacerbated this structural problem. Factors on the revenue side include:

- **Heavy reliance on property tax:** Counties must rely almost solely on property and sales taxes, while cities, for example, can collect business and utility taxes. Less diversification in the tax base means that counties are affected more severely when property tax or sales tax collections slow or drop. Property taxes make up nearly one-half of the County's general fund revenues.
- **Property-tax limiting regulation:** Initiatives such as I-747 capped increases in the property tax to one percent and was subsequently passed into law by the State

Legislature. This has limited the growth of the property tax and other revenues to under the rate of inflation.

- **A shrinking tax base due to annexations and incorporations:** Often, businesses and densely populated residential areas are annexed into cities. Consequently, their tax revenues go to cities, leaving the County with a lower level of revenue and a slower-growing base of sales tax.
- **Economic downturn:** Both property tax and sales tax collections are particularly hard hit in times of slow economic growth. Property tax revenues are depressed by the slowdown in new construction, and sales tax revenues decline dramatically as consumers cut back on spending.

Expenditures

Factors on the expenditure side include:

- **Unfunded mandates:** Although Washington State has increased the County's mandated service responsibilities, these increases rarely come with an increase in state or other funding to assist the County in meeting the additional expenses of the service requirements.
- **Urban unincorporated area services:** Although state law requires the County to be a provider of regional and rural services, the County must also provide services to several unincorporated yet heavily populated urban communities. The latter is more costly to provide because of the greater population.
- **Cost pressures:** The County faces many of the same kinds of cost pressures on its expenditures that businesses do, but has far less flexibility than many businesses to meet these challenges. For example, inflation increases the costs of providing County services, both through purchases the County makes and through rising health care costs.

Conclusion

The Council and the County Executive have adopted or advanced several measures to resolve the budget crisis in the county's general fund. But these measures do not eliminate the structural gap and the magnitude of its effect. The problems created by the structural gap can be resolved only through collaboration of the State Legislature, County, cities, and voters.



How are county services funded?

Property tax and sales tax primarily support King County's General Fund.

King County is the collector of property taxes for all taxing jurisdictions within the county. Although you pay your property tax to King County, the County receives only 18 cents of every dollar. The rest goes to other agencies, including 53 cents to schools and 19 cents to cities and towns (see first bar graph).

Similarly, with the sales tax of 9.5 cents per dollar in most of the County, the State keeps 6.5 cents, 1.8 cents goes to Metro Transit and Sound Transit, and about one cent is divided between King County and cities (second bar graph).

Legal constraints on county budget

Almost 90% of the total county budget of \$5.4 billion is restricted by law to specific purposes. These include contracts, fees, and voter-approved levies that are collected for specific uses and must be allocated toward these functions. For example, bus fares go toward paying for transit.

The flexible portion of the budget is the General Fund (12% of the total budget) that pays for traditional functions of county government, such as the Sheriff's office, and critical daily services not supported by other revenues.

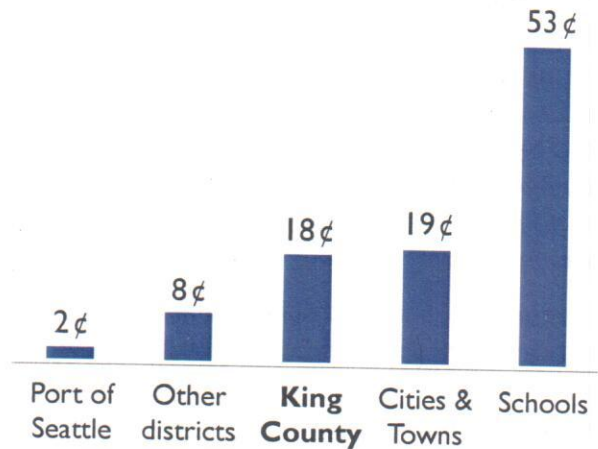
Of the General Fund, three quarters (76%) goes to pay for state-mandated criminal justice and public safety services. The remaining funds other programs for county residents, such as public health and elections.

Why is there a budget shortfall?

Counties across Washington State face a structural gap between revenue and the cost of services. While expenses rise 4-5% a year, state law limits increases in property taxes to 1% plus revenue from new construction.

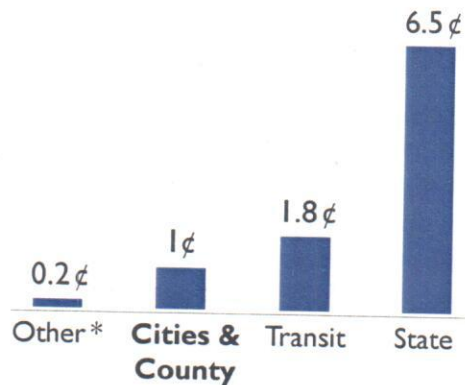
Under this cap, county revenues increase at a significantly lower rate than the rising cost of providing the same level of public services

Where your property tax dollar goes



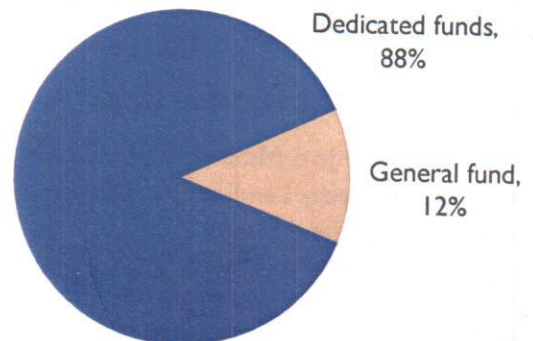
Although you pay your property taxes to King County, the County receives only 18 cents of every dollar. The rest goes to other taxing jurisdictions as shown above. (Percentages are averages for King County.)

Where your sales tax dollar goes



* Split between criminal justice, and mental health and substance abuse services.

Restricted funds



Most of the County budget is restricted by law to specific purposes. The only discretionary portion is the general fund.

(see final chart). **This difference, called the structural gap, is an ongoing challenge for all counties in our state.**

The effect of the structural gap is magnified in an economic downturn, when property tax revenues are depressed and sales tax revenues decline.

For 2013, King County faces a deficit of about \$20 million in its General Fund—the difference between the cost of services and revenue. **Counties are required by law to adopt a balanced budget. Because of the continuing effect of the structural gap, King County has been forced to cut services to residents.**

Other factors impacting the deficit, such as unfunded state mandates, are described on our web page about the budget shortfall. Please visit: www.kingcounty.gov/council/budget/budget_basics

How can the structural gap be fixed?

In the short term, the County continues to make tough decisions to balance the budget. **In the long term, the structural gap has to be addressed by the State Legislature, the County, and voters.**

Budget adoption calendar

The County Executive presented his proposed budget to the King County Council on September 24. The Council will hold three public hearings throughout the County before preparing a final budget. The budget is traditionally adopted before Thanksgiving. Below are the dates and venues of the public hearings:

October 3: Maleng Regional Justice Center
401 Fourth Avenue North, Kent

October 10: Bellevue City Hall
450 - 110th Ave NE, Bellevue,

October 17: King County Council Chambers
516 Third Ave, 10th Floor, Seattle

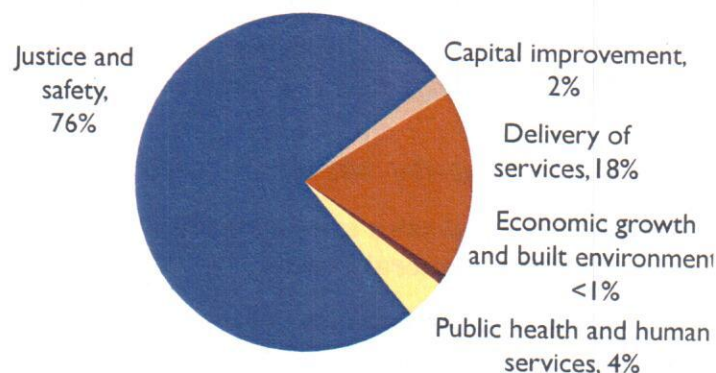
Council budget leadership

Councilmember Joe McDermott, Chair
Councilmember Kathy Lambert, Vice Chair
Council Vice Chair Jane Hague
Councilmember Julia Patterson

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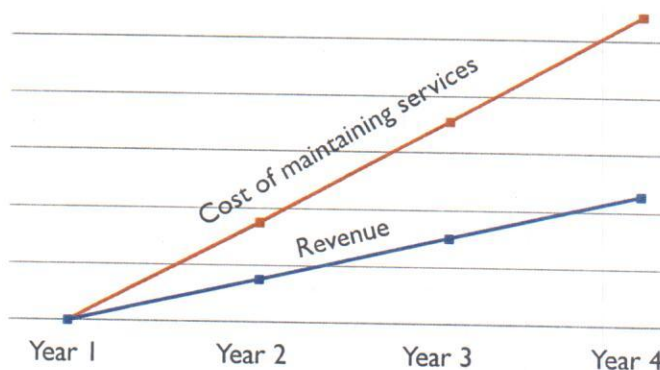
(Budget figures quoted in this brochure are current figures for 2012.)

General Fund expenditures



King County is mandated by state law to fund criminal justice and public safety services.

Effect of the structural gap



Because of the structural gap, costs of maintaining the same level of services rise at a higher percentage than limited revenue. An economic downturn worsens the situation by decreasing revenue further. This structural gap creates an ever widening deficit for all counties in Washington State.

What does my tax dollar pay for?

King County provides a range of critical services for county residents, including:

- the criminal justice system of prosecutors and public defenders, District and Superior Courts, juvenile detention and adult jails;
- the King County Sheriff's Office, which serves residents of unincorporated areas and contracts with many cities to provide police protection;
- Metro Transit bus service and county roads;
- public health and human services;
- wastewater treatment and solid waste management;
- regional parks, open space and trails; and
- elections, records, and licensing.

Myth vs. reality in the county budget

MYTH: King County hasn't cut its budget enough.

REALITY:

During the past decade, King County has cut its General Fund budget by \$384 million. Of this amount, \$233 million was cut over the past five years. This reduced funding means lower levels of service available to county residents, with cost reductions in many departments, including fewer Sheriff's deputies and deputy prosecuting attorneys, reduced support for Public Health and parks & open spaces, and little support for human services. Revenues for the unincorporated area roads fund have declined by one-fifth due to annexations, declining property values, and lower gas tax revenues, resulting in Road Services Division losing more than 100 employees, with further employee reductions expected in 2013.

MYTH: In the past, King County has threatened to cut public safety and criminal justice funds, when these should be the last to be cut.

REALITY:

King County already has cut nearly every expense from the General Fund that is not mandated by state law. Public safety and criminal justice expenses now make up 73 percent of the General Fund, not because we are spending more on them, but because everything else has been cut first. In the year 2000, criminal justice costs were just 61 percent of the General Fund.

Other services that are not mandated are funded by special levies approved by public vote—such as the Parks Levy, Roads Levy, and the Veterans & Human Services Levy—and by law cannot be used for other purposes.

MYTH: King County is not living within its means.

REALITY:

Cities have more revenue sources than counties. Cities can levy utility and business taxes, while King County's "means" or revenue sources are limited to these:

1. Property taxes, originally restricted by Initiative 747 and then by the State Legislature to increases of no more than 1 percent per year plus new construction, without voter approval. Previously, governing bodies were able to implement property tax levy increases up to 6 percent per year without voter approval. This 1-percent restriction does not cover the cost of inflation.
2. Sales taxes, which are restricted by state law and decline significantly during an economic recession.

Because of the limits on revenue sources, special tax levies are the only other way to make up the difference when revenue does not support the costs of providing services.

Beyond limitation in revenue sources, the County faces a significant challenge from the 1 percent cap on property tax increases, because the cost of maintaining the same level of services to residents rises each year at a higher rate. It is as if your salary increases very slightly, while inflation drives up the cost of rent, food, and clothing at a greater rate. As this keeps happening year after year, your ability to pay for necessities becomes less and less. This gap between the rising cost of providing services and capped revenue is called the structural gap and negatively affects all counties in Washington State.

By law, King County must have a balanced budget. As with a household, if you lose your job, you still have to pay your mortgage and utility bills. You can cut back on discretionary spending, but you still have to pay for necessities. Without adequate revenue, the county must balance its budget by reducing expenses.

King County has been able to adopt balanced budgets that include service cuts while also maintaining its AAA bond rating, which is the highest credit rating by Moody's, providing the County the lowest financing costs. Such responsible money management has kept King County solvent during the worst financial crisis in the county's and our country's history.

MYTH: Government should be run like a business.

REALITY:

If government were run like a business, then it would be able to choose its customers and refuse non-profitable requests. It would be able to exclude people who cannot pay for the services they receive, such as criminals, children, and the poor. Government must serve all residents equally, no matter how much they cost instead of contribute.

Government must follow laws that don't apply to private business and make operations more costly. Examples are complying with public records requests that consume much staff time and energy, and making proceedings open to the public. For instance, two people who serve on a three-member council or committee cannot talk about any public policy issue outside of an official, announced public meeting. These practices may not be the cheapest way of doing business, but they are required by law.

At the same time, King County is incorporating business practices in its operations, using the Lean principles to streamline operations, avoid duplication, increase efficiency, reduce costs, and improve customer service.