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INDEPENDENT AUDITOR'S REPORT

June 30, 2005

The Honorable Ron Sims, County Executive
King County
Seattle, Washington

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of King County, Washington, as of and for the year ended December 31, 2004, as listed in the table of contents. These financial statements are the responsibility of the County's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Public Transportation Fund and the Water Quality Fund, which are both major funds and represent 91 percent, 89 percent and 88 percent, respectively, of the assets, net assets, and revenues of the County's business-type activities. We also did not audit the financial statements of the Harborview Medical Center, which statements reflect 54 percent, 53 percent, and 98 percent, respectively, of the assets, net assets and revenues of the aggregate discretely presented component unit information. These financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinion, insofar as it relates to the amounts included for the Public Transportation Fund, the Water Quality Fund, and Harborview Medical Center, is based solely on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of King County, Washington, as of December 31, 2004, and the respective changes in financial position and cash flows, where applicable, thereof, and the respective budgetary comparison for the General Fund and the Public Health Fund, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

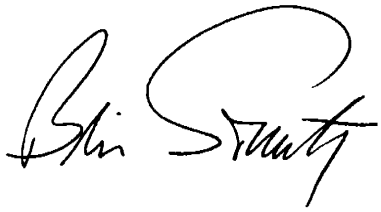
The management's discussion and analysis on pages 3 through 21 and the infrastructure modified approach information on pages 123 through 125 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. We and the other auditors have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and

presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was performed for the purpose of forming opinions on the financial statements that collectively comprise King County's basic financial statements. The accompanying information listed as combining financial statements and supplemental information on pages 127 through 249 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The combining financial statements and supplemental information have been subjected to auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the reports of other auditors, are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

The information identified in the table of contents as the Introductory and Statistical Sections is presented for purposes of additional analysis and is not a required part of the basic financial statements of the City. Such information has not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Sincerely,



BRIAN SONNTAG, CGFM
STATE AUDITOR

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of King County's (the County) Comprehensive Annual Financial Report (CAFR) presents a narrative overview and analysis of the financial activities of the County for the year ended December 31, 2004. We encourage readers to consider this information in conjunction with the additional information that is furnished in the letter of transmittal, which can be found preceding this narrative, and with the County's financial statements and notes to the financial statements, which follow.

FINANCIAL HIGHLIGHTS – PRIMARY GOVERNMENT

- As of December 31, 2004, the assets of the County exceeded its liabilities by $2,978.5 million (net assets). Because all of the County's net assets are either invested in capital assets or restricted as to use, the combined unrestricted net assets showed a $373.3 million deficit at the end of the year.
- In 2004, the County's total net assets increased by 2.4 percent or $70.9 million. The governmental net assets increased by 1.8 percent or $22.3 million, and the business-type net assets increased by 2.9 percent or $48.6 million.
- As of December 31, 2004, the County's governmental funds reported combined ending fund balances of $407.6 million. Approximately 70.9 percent or $288.8 million is unreserved fund balance available for spending at the government's discretion within the purposes specified for the County's funds.
- At the end of 2004 the unreserved, undesignated fund balance for the General Fund was $93.7 million, amounting to 20.9 percent of total General Fund expenditures for 2004. Total fund balance for the General Fund increased 27.8 percent or $26.7 million for the year.
- The County's total bonded debt increased by 13.7 percent or $343.6 million in 2004 due primarily to issuance of $164.0 million of voter approved unlimited tax general obligation bonds, $49.7 million of general obligation bonds payable from public transportation sales tax, and $185.0 million of revenue bonds, offset by $101.1 million of debt service principal payments made during the year.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the County's basic financial statements which include three components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements. This report also contains required supplementary information and other supplementary information in addition to the basic financial statements.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the County's finances in a manner similar to a private sector business. The statements provide short-term and long-term information about the County's financial position, which assists in assessing the County's financial condition at the end of the fiscal year. These statements are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This means they follow methods that are similar to those used by most businesses, taking into account all revenues and expenses connected with the fiscal year,

even if cash involved has not been received or paid. The government-wide financial statements include two statements:

The **statement of net assets** presents all of the County's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in the County's net assets may serve as a useful indicator of whether the financial position of the County is improving or deteriorating.

The **statement of activities** presents information showing how the County's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. As a result, revenues and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods, such as revenues pertaining to uncollected taxes and expenses pertaining to earned but unused vacation and sick leave.

Both of the government-wide financial statements have separate sections for three different types of county programs or activities:

Governmental activities. The activities in this section are principally supported by taxes and intergovernmental revenues. Most of the County's basic services fall into this category, including general government; law, safety and justice; physical environment; transportation; economic environment; mental and physical health; culture and recreation; and debt service. Also included within the governmental activities are the operations of the County's four flood control zone districts, of which only one is currently active. Although legally separate from the County, these component units are blended with the primary government (King County) because of their governance relationship with the County.

Business-type activities. These functions are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type activities include the operation of the County's public transportation system, wastewater treatment facilities, solid waste disposal facilities, airport, and other services.

Discretely presented component units. The government-wide financial statements include not only King County itself as the primary government, but also three legally separate entities for which the County is financially accountable: the Harborview Medical Center (HMC), the Washington State Major League Baseball Stadium Public Facilities District (PFD), and the Cultural Development Authority (CDA) of King County, doing business as 4Culture. Financial information for these component units is reported separately from the financial information presented for the primary government itself in a single, aggregated presentation in the government-wide financial statements. Individual financial statements for each component unit can be found immediately following the fiduciary funds financial statements in the Basic Statements section of this report.

Fund Financial Statements

The fund financial statements are designed to report information about groupings of related accounts that are used to maintain control over resources that have been segregated for specific activities or objectives. The County, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the County can be divided into three categories: **governmental** funds, **proprietary** funds, and **fiduciary** funds.

Governmental funds. Most of the basic services provided by the County are financed through governmental funds. Governmental funds are used to account for essentially the same functions that are reported as governmental activities in the government-wide financial

statements. Unlike the government-wide financial statements, however, the governmental funds financial statements focus on: (1) how cash and other financial assets can readily be converted to available resources; and (2) the balances left at year-end that are available for spending. Such information may be useful in determining whether there will be adequate financial resources available to meet the current needs of the County.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The County maintains a general fund and several other individual governmental funds organized according to their type (special revenue, debt service, and capital projects). Three governmental funds, the General Fund, the Public Health Fund, and the Harborview Medical Center Bond Administration Fund are considered to be major funds for financial reporting purposes. Each of the major funds is presented in a separate column in the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances. Data from the other governmental funds are combined into a single, aggregated presentation. Individual fund data for each of these nonmajor funds is provided in the form of combining and subcombining statements in the Governmental Funds section of this report, following the Basic Statements section.

The County adopts an annual budget appropriated at the department/division level for the General Fund and at the fund level for the Public Health Fund. A budgetary comparison statement has been provided for the two major governmental funds with an annual budget. The third major governmental fund is not a budgeted fund.

The basic governmental funds financial statements can be found immediately following the government-wide statements.

Proprietary funds. Proprietary funds are generally used to account for services for which the County charges customers a fee. Proprietary funds provide the same type of information as shown in the government-wide financial statements, only in more detail. Like the government-wide financial statements, proprietary funds financial statements use the accrual basis of accounting. The basic proprietary funds financial statements can be found immediately following the governmental funds financial statements.

The County maintains the following two types of proprietary funds:

Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The proprietary funds financial statements provide separate information for the Water Quality Enterprise and the Public Transportation Enterprise, both considered to be major funds of the County for financial reporting purposes. All other enterprise funds are aggregated into a single presentation within the proprietary funds financial statements.

Internal service funds are used to report activities that provide services to the County's other programs and activities on a cost reimbursement basis. The County uses internal service funds to account for its motor pool, information and telecommunications services, facilities management, risk management, employee benefits, and financial and various

other administrative services. These services predominantly benefit governmental rather than business-type functions and have been included within governmental activities in the government-wide financial statements. One internal service fund that provides equipment and fleet maintenance and procurement for the Water Quality Enterprise is included within the business-type activities in the government-wide financial statements but is combined with all other internal service funds into a single aggregated presentation in the proprietary funds financial statements.

Individual fund data for each of the nonmajor proprietary funds is provided in the form of combining statements found in the Proprietary Funds section of this report.

Fiduciary funds. Fiduciary funds are used to account for resources held for the benefit of parties outside the government. Fiduciary funds include the investment trust funds, used to report investment activity conducted by the County on behalf of legally separate entities, such as special districts and public authorities that are not part of the County's reporting entity, and the agency funds. Since the resources of these funds are not available to support the County's own programs, they are not reflected in the government-wide financial statements. The accounting used for fiduciary funds is much like that used for proprietary funds. The basic fiduciary funds financial statements can be found immediately following the proprietary funds financial statements.

Individual fund data for each of the fiduciary funds is provided in the form of combining statements that can be found in the Fiduciary Funds section of this report.

Notes to the financial statements

The notes provide additional information essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the financial statements can be found immediately following the individual component unit financial statements in the Basic Statements section of this report.

Other information

Required supplementary information. In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information on infrastructure assets reported using the modified approach. The required supplementary information immediately follows the notes to the financial statements in the Basic Statements section of this report.

Combining Statements. The combining and subcombining statements, referred to earlier, are presented in separate sections immediately following the required supplementary information.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

Analysis of Net Assets

Net assets may serve over time as a useful indicator of a government's financial position. As indicated in the condensed financial information on the following page, which was derived from the government-wide Statement of Net Assets, the County's combined net assets (governmental and business-type activities) were $2,978.5 million at the end of 2004. This is an increase of 2.4 percent or $70.9 million over the net assets of the previous year, as restated.

Governmental activities. Although net assets of the County's governmental activities increased 1.8 percent to $1,246.2 million, all of the net assets are either subject to external restrictions as to how they may be used, or are invested in capital assets (e.g., land, buildings, infrastructure,

right-of-way, equipment, and work in progress) less any related outstanding debt used to acquire those assets. Consequently, unrestricted net assets for governmental activities showed a $460.4 million deficit at the end of 2004. This is a 31.0 percent or $109.0 million increase in the deficit in unrestricted net assets over that of fiscal year-end 2003 due primarily to the issuance of $164.0 million of voter-approved unlimited tax general obligation bonds and the transfer of the bond proceeds to the Harborview Medical Center.

Net Assets as of December 31, 2004

(in millions)

	Governmental Activities		Business-type Activities		Total	
	2004	2003[a]	2004	2003	2004	2003
Assets:						
Current and other assets	$ 785.9	$ 723.9	$ 676.5	$ 743.8	$ 1,462.4	$ 1,467.7
Capital assets	2,054.2	1,857.0	3,256.0	2,967.9	5,310.2	4,824.9
Total Assets	2,840.1	2,580.9	3,932.5	3,711.7	6,772.6	6,292.6
Liabilities:						
Long-term liabilities	1,399.6	1,113.6	1,955.8	1,776.4	3,355.4	2,890.0
Other liabilities	194.3	243.4	244.4	251.6	438.7	495.0
Total Liabilities	1,593.9	1,357.0	2,200.2	2,028.0	3,794.1	3,385.0
Net Assets:						
Invested in capital assets, net of related debt	1,448.9	1,316.2	1,362.1	1,220.5	2,811.0	2,536.7
Restricted	257.7	259.1	283.1	360.7	540.8	619.8
Unrestricted	(460.4)	(351.4)	87.1	102.5	(373.3)	(248.9)
Total net assets	$ 1,246.2	$ 1,223.9	$ 1,732.3	$ 1,683.7	$ 2,978.5	$ 2,907.6

(a) Current and other assets, Other liabilities, and Unrestricted net assets have been restated, see Note 15, "Restrictions, Reserves, Designations, and Changes in Equity" – Restatements of Beginning Balances.

This deficit does not mean that the County's governmental activities do not have resources available to pay their obligations in the coming year. The increase in net assets for governmental activities in 2004 reflects the County's ability, on an annual basis, to meet its current obligations in those activities including the related debt service requirements. The deficit in the unrestricted net assets is the result of the governmental activities having long-term commitments that are greater than currently available resources. Specifically, the County's governmental activities include general obligation debt of $604.7 million, $125.8 million more than at the end of 2003, for which no corresponding assets are recorded but for which future revenues are obligated.

Of the amount of debt with no corresponding assets, 75.7 percent or $457.9 million is related to assets that are recorded on the books of two of the County's three discretely presented component units: the Washington State Major League Baseball Stadium PFD ($226.9 million), and the Harborview Medical Center ($231.0 million). As discretely presented component units, these entities are not part of the primary government or incorporated into this analysis. The remainder of the debt, for which there are no corresponding assets, consists of $113.4 million

associated with the Kingdome facility, which was demolished to make room for the Seahawks (Qwest) Football Stadium, and $33.4 million used to finance assets that have been contributed by the County to other programs and services that benefit the citizens of the County.

Business-type activities. There was an increase of 2.9 percent to $1,732.3 million in net assets of the business-type activities. Of the total net assets for business-type activities, 78.6 percent or $1,362.1 million is invested in capital assets (e.g., land, buildings, vehicles, plant assets, equipment, and work in progress), net of related debt. This is an increase of $141.6 million over 2003 due primarily to the significant capital asset acquisitions by the Public Transportation Enterprise in 2004. The business-type activities use these capital assets to provide services to their customers; consequently, these assets are not available for future spending. The resources needed to repay the debt incurred to acquire these assets must be provided from other sources since the capital assets themselves cannot be liquidated for these liabilities. Another 16.4 percent of the total net assets for the business-type activities is restricted as to use for capital construction ($181.2 million), debt service ($100.4 million), and other purposes ($1.5 million). The remaining 5.0 percent or $87.1 million is unrestricted net assets that may be used to finance the continuing operations of the County's business-type activities. Any balance in the unrestricted net assets for business-type activities cannot be used to reduce the unrestricted net asset deficit in governmental activities.

The combination of the $460.4 million deficit in the governmental activities unrestricted net assets and the $87.1 million positive balance in the business-type activities unrestricted net assets resulted in the deficit of $373.3 million in total unrestricted net assets for the County as a whole.

Analysis of Changes in Net Assets

The increase in 2004 in the County's total net assets resulted from revenues exceeding related expenses and reflects the County's ability to meet its ongoing obligations including its debt service requirements. Approximately 41.6 percent of the County's total revenues came from taxes, primarily Property tax and the Retail sales and use tax. Charges for various goods and services provided 39.2 percent of the total revenues, while 17.9 percent was derived from operating and capital grants and contributions (including state and federal assistance). The County's expenses cover a range of services, the largest of which were for law, safety and justice; mental and physical health; public transportation; and water quality.

The condensed financial information on the following page is derived from the government-wide Statement of Activities and reflects how the County's net assets changed during the 2004 fiscal year.

Governmental activities. Governmental activities accounted for 31.5 percent of the total growth in net assets of the County, resulting in an increase in the County's governmental activities net assets of $22.3 million. Program revenues for governmental activities total $726.7 million and include the amount paid by those who directly benefited from the programs ($447.3 million), and by other governments and organizations that subsidized certain programs with operating grants and contributions ($182.3 million), and capital grants and contributions ($97.1 million). In 2004 the cost of all governmental activities was $1,352.5 million. The County paid for the $625.8 million remaining "public benefit" portion of governmental activities with $433.6 million in property taxes, $128.6 million in retail sales and use taxes, and $85.4 million in other revenues including other taxes and interest earnings. As discussed earlier, all of the increase in governmental activities net assets was either restricted as to use or used to acquire capital assets to provide services to the County's citizens.

Changes in Net Assets
For the Year Ended December 31, 2004
(in millions)

	Governmental Activities		Business-type Activities		Total	
	2004	2003[a]	2004	2003	2004	2003
Revenues:						
Program revenues:						
Charges for services	$ 447.3	$ 432.9	$ 442.5	$ 422.5	$ 889.8	$ 855.4
Operating grants and contributions	182.3	198.6	35.7	24.3	218.0	222.9
Capital grants and contributions	97.1	103.7	91.4	53.8	188.5	157.5
General revenues:						
Property taxes	433.6	394.9	-	-	433.6	394.9
Retail sales and use taxes	128.6	121.2	314.2	296.7	442.8	417.9
Other taxes	67.0	59.6	-	-	67.0	59.6
Unrestricted interest earnings	18.4	20.2	9.7	10.9	28.1	31.1
Total revenues	1,374.3	1,331.1	893.5	808.2	2,267.8	2,139.3
Expenses[b]						
General government [c]	79.6	53.6	-	-	79.6	53.6
Law, safety and justice	475.1	491.8	-	-	475.1	491.8
Physical environment	58.0	52.4	-	-	58.0	52.4
Transportation	70.8	64.7	-	-	70.8	64.7
Economic environment	76.3	80.4	-	-	76.3	80.4
Mental and physical health [d]	504.3	327.2	-	-	504.3	327.2
Culture and recreation	39.0	36.4	-	-	39.0	36.4
Interest and other debt service costs	49.4	46.0	-	-	49.4	46.0
Airport	-	-	12.3	11.6	12.3	11.6
Public transportation	-	-	508.3	463.3	508.3	463.3
Solid waste	-	-	78.0	79.0	78.0	79.0
Water quality	-	-	239.6	229.6	239.6	229.6
Other enterprises activity	-	-	6.2	6.2	6.2	6.2
Total expenses	1,352.5	1,152.5	844.4	789.7	2,196.9	1,942.2
Increase in net assets before transfers	21.8	178.6	49.1	18.5	70.9	197.1
Transfers	0.5	2.5	(0.5)	(2.5)	-	-
Increase in net assets	22.3	181.1	48.6	16.0	70.9	197.1
Net assets, beginning of year (Restated)	1,223.9	1,042.8	1,683.7	1,667.7	2,907.6	2,710.5
Net assets, end of year	$ 1,246.2	$ 1,223.9	$ 1,732.3	$ 1,683.7	$ 2,978.5	$ 2,907.6

(a) Net assets, beginning of year has been restated, see Note 15, "Restrictions, Reserves, Designations, and Changes in Equity" – Restatements of Beginning Balances.

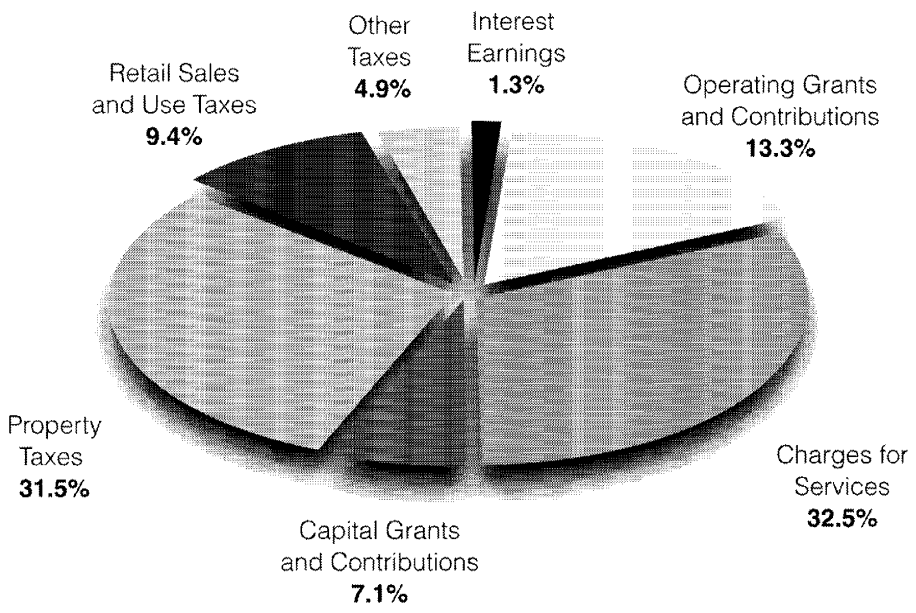
(b) Expenses for all functions include the allocation of indirect expenses from the general government function. The amount of indirect general government expenses allocated to each function is shown in a separate column on the County's government-wide Statement of Activities alongside the column that reflects the direct operating expenses incurred by each function. As a result of this allocation, the $79.6 million in General government expense above consists of $101.3 million in direct program expenses and loss on disposal (transfer) of capital assets of $38.0 million reduced by a net allocation of $59.7 million to other County functions.

(c) General government expenses includes loss on sale of capital assets of $38.0 million and $1.3 million in 2004 and 2003, respectively. The 2004 loss on sales of capital assets was primarily due to the loss related to the transfer of road infrastructure and land to cities ($23.9 million) due to annexations and the loss related to the transfer of Park land and buildings to cities ($9.4 million).

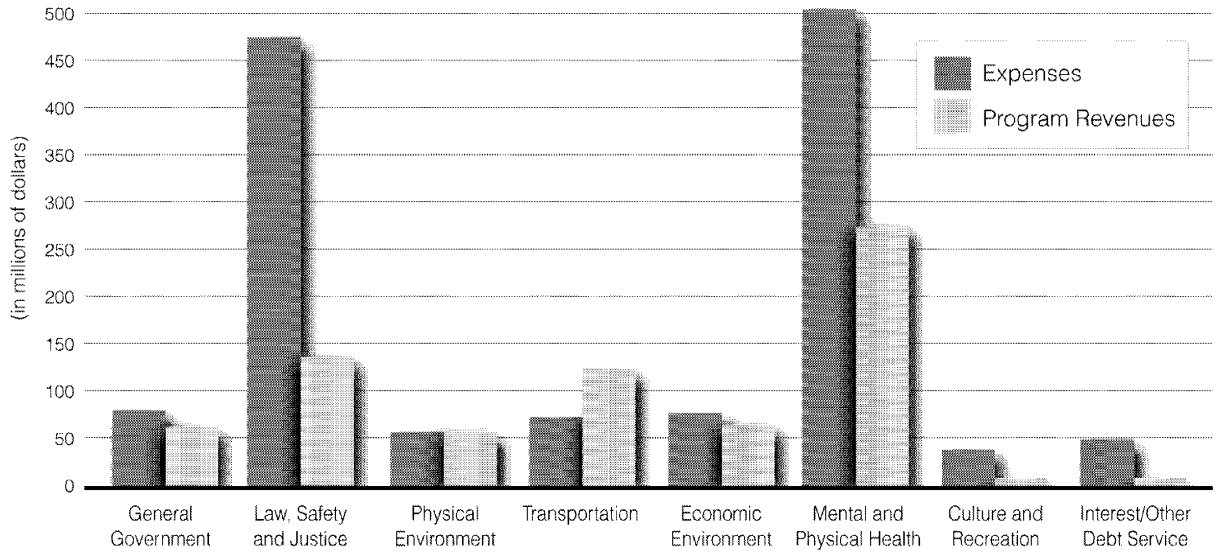
(d) 2004 Mental and physical health expenses includes $165.3 million of expenses related to the issuance of unlimited tax general obligation bonds for the component unit Harborview Medical Center (HMC). While King County retains the liability for the bonds, the bond proceeds were transferred to HMC.

The charts below illustrate the County's revenues by source and its expenses and program revenues by function for its governmental activities:

Revenues by Source - Governmental Activities



Expenses and Program Revenues - Governmental Activities



Charges for services provided 32.5 percent, and property taxes 31.5 percent, of total revenues for governmental activities. One of the most significant expense amounts is for Law, safety and justice, a function that requires the greatest usage of general government revenues. The primary revenue sources for Mental and physical health are charges for services and operating grants and contributions, which paid for 53.8 percent of the activities for that function. In 2004 Transportation received $44.4 million in infrastructure capital assets and $24.8 million in right-of-way from other local governments, capital contributions that enabled program revenues to exceed expenses. The expense related to the transfer of $26.7 million in book value of road infrastructure and right-of-way ($23.9 million net of proceeds from the sale of road capital assets) to cities due to annexations has been reported as an expense of the General Government function.

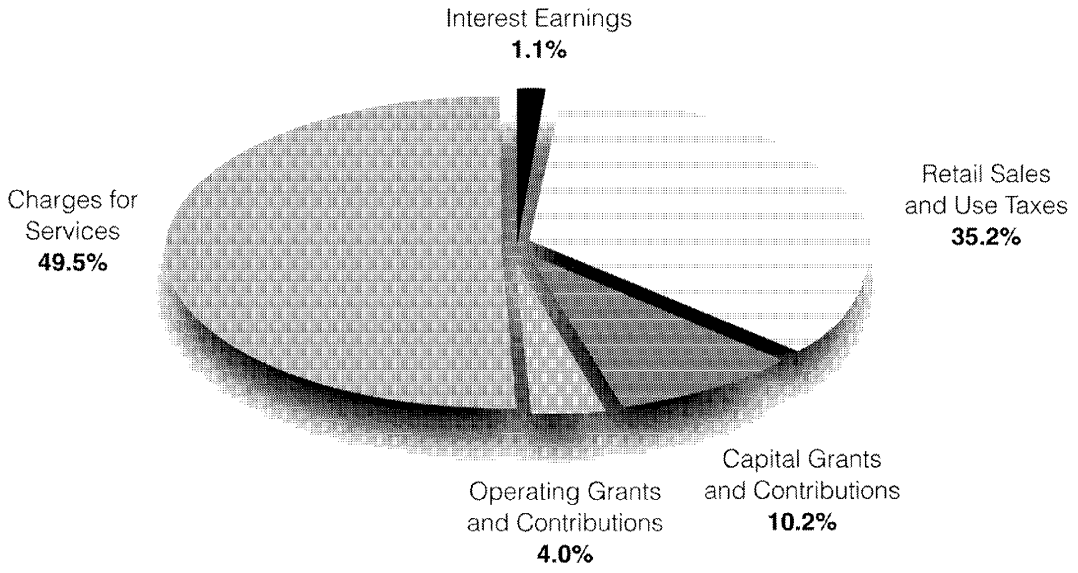
A comparison of the cost of services by function for the County's governmental activities is shown below, along with the revenues used to cover the net expenses of the governmental activities (expressed in millions):

(Expenses) Net of Program Revenues:	
General government	$ (18.9)
Law, safety and justice	(341.4)
Physical environment	0.3
Transportation	54.0
Economic environment	(13.9)
Mental and physical health	(232.7)
Culture and recreation	(32.1)
Interest and other debt service costs	(41.0)
Total expenses	(625.7)
General revenues:	
Property taxes	433.6
Retail sales and use taxes	128.6
Other taxes	66.9
Unrestricted interest earnings	18.4
Other	0.5
Increase in net assets	$ 22.3

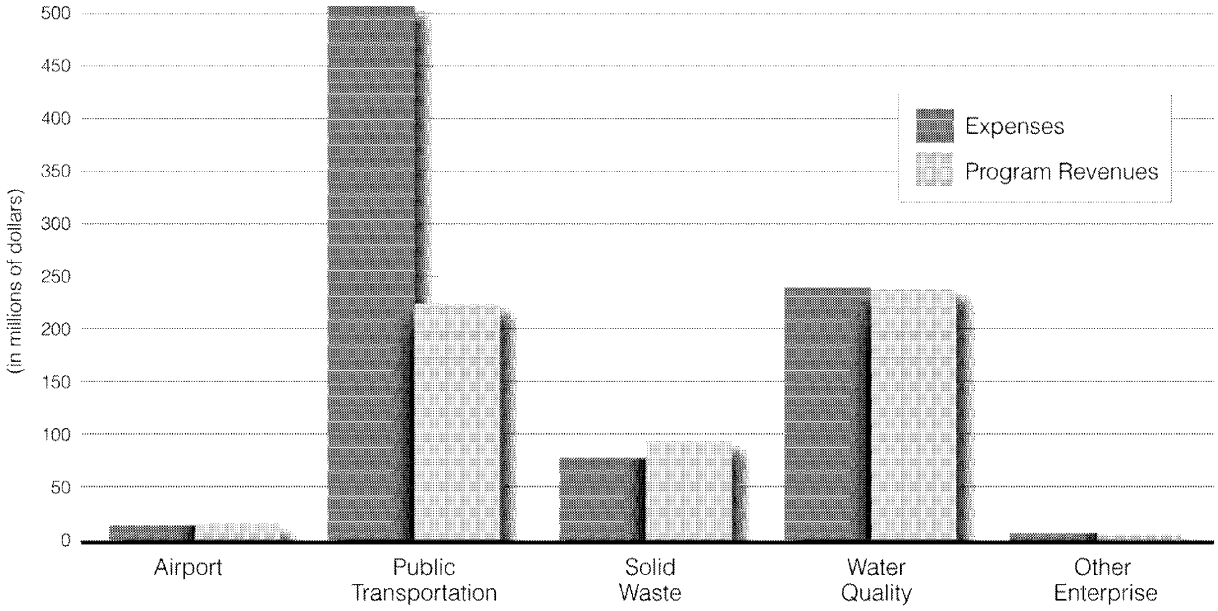
Business-type activities. Business-type activities increased the County's net assets by $48.6 million in 2004, accounting for 68.5 percent of the total growth in net assets of the County. Total revenues for business-type activities were $893.5 million. The cost of all business-type activities for 2004 was $844.4 million. Of that amount, 67.5 percent or $569.6 million was funded from program revenues, including $442.5 million in charges for services, $35.7 million from other governments and organizations that subsidized certain programs with operating grants, and $91.4 million in capital grants and contributions. The Public Transportation program operations are subsidized with Retail sales and use tax revenues, which amounted to $314.2 million in 2004. In addition, the business-type activities received $9.7 million in unrestricted interest earnings and other general revenue.

The charts on the following page illustrate the County's business-type revenues by source and business-type expenses and program revenues by function:

Revenues by Source - Business-type Activities



Expenses and Program Revenues - Business-type Activities



FINANCIAL ANALYSIS OF THE COUNTY'S FUNDS

As noted earlier, the County uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

The focus of the County's governmental funds is to provide information on near-term inflows, outflows, and balances of resources that are available for spending. Such information is useful in assessing the County's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net financial resources available for spending at the end of the fiscal year.

At December 31, 2004, the County's governmental funds reported combined ending fund balances of $407.6 million, an increase of $71.9 million in comparison with the prior year after restating beginning fund balance. Approximately 70.9 percent ($288.8 million) constitutes unreserved fund balance which is available for spending in the coming year at the County's discretion. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has already been committed to the liquidation of outstanding contracts and purchase orders of the prior fiscal year ($90.1 million), to pay debt service ($15.8 million), for asset prepayments ($4.1 million), and for a variety of other restricted purposes ($8.8 million).

Overall governmental fund revenues totaled approximately $1,356.8 million for 2004, which represents an increase of 4.5 percent or $57.9 million over the fiscal year ended December 31, 2003. The increase was primarily due to strong growth in Property taxes ($40.1 million) and Retail sales and use taxes ($7.4 million). In 2004 expenditures for governmental funds totaled $1,613.4 million, an increase of 17.7 percent or $242.5 million from the previous fiscal year. This large increase includes one-time expenditures of $165.3 million related to the transfer to HMC of the proceeds of two Unlimited Tax General Obligation Bond Issues used to finance seismic upgrades and public health and safety improvements for Harborview Medical Center (HMC) and the King County Medical Examiner's Office, and $62.5 million related to the acquisition of an office building via capital lease. Excluding these one-time expenditures, expenditures were up 1.1 percent or $14.6 million from the previous fiscal year, an increase of $14.1 million (1.3 percent) in Current expenditures, $12.4 million (10.4 percent) in Debt Service expenditures, and a decrease of $11.9 million (7.9 percent) in Capital Outlay expenditures. Total expenditures for governmental funds exceeded revenues by $256.6 million in 2004 compared to $72.0 million for the 2003 fiscal year.

The **General Fund** is the chief operating fund for the County. At the end of the fiscal year, total fund balance for the General Fund equaled $123.0 million. Unreserved fund balance, the amount considered available to spend, totaled $115.1 million. Of that amount, $21.4 million has been designated for working capital purposes and contingencies and is not considered available to spend. As a measure of the General Fund's liquidity, it may be useful to compare both unreserved fund balance and total fund balance to total fund expenditures. Unreserved fund balance represents 25.7 percent of total General Fund expenditures, a considerable increase from the 18.8 percent of a year ago. Total fund balance represents 27.4 percent of total General Fund expenditures, an increase from the 20.7 percent of a year ago.

The fund balance of the County's General Fund increased by $26.7 million during the current fiscal year. Key factors in this growth are as follows:

- Revenues grew by $24.8 million (4.9 percent) due primarily to an increase of $15.4 million in taxes (a $10.1 million increase in property taxes revenues and $4.2 million from additional retail sales and use taxes), a $6.1 million increase in Intergovernmental

Revenues and an increase of $6.6 million in Miscellaneous Revenues. A comprehensive review of county operations, conducted as part of the 2004 budget preparation, determined that the Solid Waste Enterprise should make an annual lease payment of $7 million to the General Fund for the use of the Cedar Hills property as a regional landfill.

- Expenditures actually declined in 2004 as 2003 expenditures included $20.3 million of one-time litigation expenditures. Another change from 2003 is the transfer of the operations and maintenance of regional parks and trails from the General Fund to the new Parks and Recreation Fund. In May 2003 voters approved a County-wide four-year temporary Property tax lid lift for Regional and Rural Parks at a rate not to exceed $0.049 per $1,000 of assessed value. As a result, General Fund expenditures of $16.2 million in 2003 for parks and recreation fell to zero in 2004. Excluding those two factors, General Fund expenditures were up $19.4 million (an increase of 4.5 percent); $13.6 million of that increase was due to increased spending on Law, Safety and Justice (including Jail Health). In 2004, the County changed the way the cost of Jail Health is budgeted and reported. In prior years, the cost of Jail Health had been included in the Department of Adult and Juvenile Detention (Law, Safety and Justice) expenditures. Beginning in 2004, the cost of providing healthcare to inmates was budgeted and reported in Jail Health under the expenditure function Mental and physical health to provide more transparency to this important function.

- The $79.3 million in excess revenues over expenditures was reduced by $52.6 million in other financing uses which had increased by $20.2 million from the previous year due to increased support of other funds by the General Fund. This includes $3.6 million increased support for the Building Repair and Replacement Fund, $4.0 million increased support for the Major Maintenance Reserve Fund, $5.7 million increased support for the Office of Information Resource Management Capital Fund and $3.0 million for the new Parks and Recreation Fund.

The **Public Health Fund**, a special revenue fund, is used to finance health service centers located throughout the County and other public health programs to promote health and prevent disease to King County residents. At the end of 2004 it had a total fund balance of $10.6 million, of which $7.0 million was unreserved and available for spending. Revenues and expenditures in 2004 were lower than in 2003 due to the aforementioned transfer of Jail Health from Public Health to the General Fund. After adjusting 2003 amounts for the change, total revenues increased $12.2 million in 2004 from the 2003 level. However, the adjusted increase in expenditures in 2004 was $14.1 million. As a consequence of the increase in the cost of providing health services over the County's ability to fund those services with intergovernmental revenues or charges for services, the total fund balance of the Public Health Fund declined by $3.1 million to $10.6 million. With the increased need for Public Heath services in combination with revenues not keeping pace with the increases in related costs, the Public Health Fund is continuously working to find efficiencies to improve productivity in its delivery of health services.

The **Harborview Medical Center Bond Administration Fund**, a capital projects fund, was used to account for the 2004 receipt of bond proceeds in the Primary Government as an *other financing source*, and the effective expenditure to reflect the application of the bond proceeds as a capital contribution to Harborview Medical Center in compliance with generally accepted accounting principles. In 2004 $164.0 million of unlimited general obligation bonds were issued for construction and improvements to building and facilities used by Harborview Medical Center. A total of $193.0 million in bond proceeds have been issued

since 2001. Additional funding is expected to be provided from Harborview Medical Center revenues and grants.

Proprietary Funds

The County's proprietary funds provide the same type of information found in the government-wide financial statements for business-type activities. This information is presented on the same basis of accounting, but provides more detail.

As discussed in the business-type activities above, the County's net assets increased by $48.6 million as a result of operations in the proprietary funds adjusted to reflect the consolidation of internal service fund activities related to the enterprise funds. Of the two major proprietary funds, the Public Transportation Enterprise provided $53.6 million of this increase while the net assets of the Water Quality Enterprise increased by $2.2 million.

The **Public Transportation Enterprise** accounts for the operations, maintenance, capital improvements, and expansion of public transportation and related facilities in the County under the King County Transit Division. At the end of 2004 the Public Transportation Enterprise had total net assets of $1,203.8 million of which 83.1 percent or $999.8 million was invested in capital assets, net of related debt; 14.2 percent or $171.3 million was restricted as to use for capital purposes and bond reserves; and 2.7 percent or $32.7 million was unrestricted and available for spending. Net assets increased by $53.6 million in 2004, a significant increase from the $9.5 million increase recorded in 2003. The 2004 increase was principally attributable to Federal funding of the acquisition of 213 hybrid diesel-electric articulated 60-foot low-floor buses. In updating its fleet, Public Transportation retired more than 200 buses and numerous vans and small buses. During 2004, Public Transportation experienced the effect of increased diesel prices, paying an average of $1.39 per gallon, resulting in additional fuel expenditures of $4.5 million over the budgeted estimate.

The **Water Quality Enterprise** accounts for the operation, maintenance, capital improvements, and expansion of the County's water pollution control facilities under the King County Wastewater Treatment Division. Total net assets in the enterprise fund were $339.9 million at the end of 2004 of which 62.4 percent or $212.1 million was invested in capital assets, net of related debt; 28.1 percent or $95.4 was restricted as to use for construction projects and debt service; and the remaining 9.5 percent or $32.4 million was unrestricted and available for spending. Operations of the Water Quality Enterprise were stable during 2004 with operating expenses net of depreciation declining $0.1 million between 2003 and 2004. The monthly sewer rate was unchanged (2004 is the third year of a planned three-year level rate for monthly sewer charges). Total sewer rate revenues rose $1.0 million, reflecting an overall 0.4 percent increase in the sewer rate customer base. Capacity charge revenues increased $1.2 million, reflecting a higher rate in 2004 and the addition of 11,136 new connections.

General Fund Budgetary Highlights

The County's final General Fund budget differs from the original budget in that it reflects an anticipated increase in appropriations of $10 million. However, actual expenditures incurred were $11.4 million less than the original budget resulting in an underutilization of the total final appropriation authority by $21.4 million — $9.3 million underexpenditures in general governmental services; $5.4 million in law, safety and justice; and $5.2 million in transfers out. During the year total revenues exceeded budgetary estimates by $23.6 million and total expenditures were less than budgetary estimates by $21.4 million, eliminating the need to draw upon the existing fund balance. The underexpenditure of $1.7 million by Records, Elections and Licensing Division, a General Fund agency, is due to savings related to the cancellation of the Presidential Preference Primary and a grant from the State of Washington to fund the implementation costs of the new state primary system.

The County's fiscal policies provide that the ending undesignated budgetary fund balance for the general fund should be planned at between six and eight percent of estimated annual revenues. The ending undesignated fund balance on the General Fund budgetary basis financial plan for 2004 was $27.2 million.

CAPITAL ASSETS, INFRASTRUCTURE, AND DEBT ADMINISTRATION

Capital assets

The King County primary government's investment in capital assets for its governmental and business-type activities as of December 31, 2004, amounts to $5,310.2 million (net of accumulated depreciation). Capital assets include land, right-of-way, farmland development rights, buildings, improvements other than buildings, roads and bridges infrastructure, vehicles, machinery and equipment, furniture, and construction in progress. The total increase in the investment in capital assets over 2003 was 10.1 percent (10.6 percent increase for governmental activities and 9.7 percent increase for business-type activities).

Major capital asset events during 2004 included the following:

- Governmental capital land increased by 7.6 percent. A notable acquisition is for development rights in Snoqualmie Forest for $22.5 million under the County's forest preservation program. Also significant is the cost of infrastructure right-of-way assets turned over to the County by private developers amounting to $24.7 million.

- The County added to its governmental capital building facilities through construction and capital lease financing. The Kent Pullen Regional Communications and Emergency Coordination Center in Renton was completed during the year at a cost of $24.0 million and a capital lease financing agreement for the Patricia Bracelin Steel Memorial Building in Seattle was consummated, with the total property value at $62.5 million. The project to retrofit the King County Courthouse Facility for seismic and code required life and safety system was also completed at a cost of about $75.0 million.

- Technology spending continued at a brisk pace as the County pushed through with its programs for upgrading computer hardware and for developing information systems that will enhance business processes. About $16.8 million was spent county-wide on new and replacement personal computers, servers, and network-related equipment.

- Capital assets of the Transportation Enterprise increased by $164.3 million or 16.2 percent over 2003. The change is primarily attributable to the purchase of replacement vehicles and an increase in capitalized work in progress due to the ongoing implementation of the enterprise's capital improvements plan. Transit's capital improvement program involves systemwide improvement and expansion, additions to the bus fleet, base expansions and modifications, and acquisition and development of park-and-ride facilities.

- Capital assets of the Water Quality enterprise increased by $110.1 million or 6.2 percent over 2003. The change is a result of replacement and additions to the interceptor and siphon systems, purchases of land, additional storage capacity, extensions of sewer trunk lines, and continued efforts to control odor and improve sewage-handling technology. Construction work in progress increased by $153.0 million or 33.7 percent from the continued implementation of the Enterprise's Regional Wastewater Services Plan.

More detailed information on the County's capital assets can be found in Note 6 – Capital Assets.

King County Capital Assets
(net of accumulated depreciation)
(in millions)

	Governmental activities		Business-type activities		Total	
	2004	2003	2004	2003	2004	2003
Land	$ 635.8	$ 590.7	$ 243.1	$ 225.5	$ 878.9	$ 816.2
Buildings and improvements	482.3	344.6	1,410.6	1,382.1	1,892.9	1,726.7
Infrastructure	800.8	714.0	-	-	800.8	714.0
Equipment	83.9	89.9	817.2	731.1	901.1	821.0
Construction in progress	51.4	117.8	785.1	629.2	836.5	747.0
Total	$ 2,054.2	$ 1,857.0	$ 3,256.0	$ 2,967.9	$ 5,310.2	$ 4,824.9

Infrastructure

The County has elected to use the modified approach as defined in GASB Statement No. 34 for infrastructure reporting for its roads and bridges. Under the modified approach, asset condition is reported rather than recording depreciation. The rating scales for pavements (roads) and bridges are further explained in the required supplementary information, which follows the notes to the basic financial statements.

The County performs condition assessments on its network of roads through the King County Pavement Management System, which generates a Pavement Condition Index (PCI) for each segment of arterial and local access road in the network. The PCI is a numerical index on a 100-point scale that represents the pavement's functional condition based on the quantity, severity, and type of visual distress. Condition assessments are undertaken every three years.

It is the policy of the King County Roads Division to maintain at least 80 percent of the road system at a PCI of 40 or better. In the most recent condition assessments, 87.8 percent of the arterial roads in the County and 88.5 percent of the local access roads in the County had a PCI rating at 40 and above. The majority of roads that fall below the established rating are local access roads that are situated in rural areas. The amount budgeted in 2004 for road maintenance was $31.2 million. The amount actually expended was $29.1 million. Underspending of the budgeted amount is a result of the removal of roads from the project list because of conflicts with anticipated utility work, cost efficiencies related to a relatively few roads to be resurfaced in remote locations, and weather-related work reductions or stoppages.

The County currently maintains 181 bridges. Physical inspections to uncover deficiencies are carried out at least every two years and documented in an inspections report. There is also an annual evaluation to determine which bridges are candidates for replacement or rehabilitation using a 10-point priority scale based on various factors of bridge condition. A key element in the priority scale is the sufficiency rating, which is a numerical rating (on a 100-point scale) of a bridge based on its structural adequacy and safety, essentiality for public use, and its serviceability and functional obsolescence. The policy of the King County Roads Division is to maintain bridges in such a manner that no more than 12 (6.6 percent) will have a sufficiency rating of 20 or less. As of December 31, 2004, there were 9 bridges in this category. The amount budgeted in 2004 to maintain and preserve bridges was $4.0 million. Actual amounts expended were $3.1 million.

Debt Administration

As of December 31, 2004, King County Primary Government has total bonded debt outstanding of $2,860.9 million for its governmental and business-type activities. Of this amount, $1,650.6 million is comprised of debt backed by the full faith and credit of the County. The $1,210.3 million remainder of the County's bonded debt represents bonds secured solely by specified revenue sources (i.e., revenue bonds).

King County's Outstanding Debt
General Obligation and Revenue Bonds
(in millions)

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
General obligation bonds	$ 1,043.3	$ 870.3 [a]	$ 560.9	528.8	$ 1,604.2	$ 1,399.1
General obligation bond anticipation notes	46.4	80.0	-	-	46.4	80.0
Special assessment debt with governmental commitment	-	0.1	-	-	-	0.1
Revenue bonds	-	-	1,210.3	1,038.1	1,210.3	1,038.1
Total	$ 1,089.7	$ 950.4	$ 1,771.2	$ 1,566.9	$ 2,860.9	$ 2,517.3

(a) Restated, consistent with 2004, to include bonds payable from component units' resources. See Note 13, "Debt " – Changes in Long-term Liabilities.

In 2004 the County's total bonded debt increased by 13.7 percent or $343.6 million. In the governmental activities, the bonded debt increased by 14.7 percent or $139.3 million, primarily due to $164.0 million of voter-approved unlimited tax general obligation bonds issued to provide funding for the seismic improvements to the Harborview Medical Center. In the business-type activities, the key factors for the increase of bonded debt by 13.0 percent or $204.3 million were the issuance of $185.0 million of sewer revenue bonds to finance the Wastewater Treatment Division's capital needs and the issuance of $49.7 million of general obligation bonds payable from public transportation sales tax to finance the Transit Division's capital improvement program.

In addition, the County refinanced some of its existing debt during the fiscal year to take advantage of lower interest rates through advance refunding:

- The County refinanced $57.0 million of general obligation bonds that is expected to decrease future aggregate debt service payments by $4.5 million over the life of the bonds.
- The County refinanced $54.3 million of previously outstanding general obligation (baseball stadium) bonds by providing $13.0 million of excess proceeds from special taxes and revenues and issuing $45.3 million of general obligation (baseball stadium) bonds. The result of the refunding is expected to decrease future aggregate debt service payments by $24.8 million over the life of the bonds.
- The County also refinanced $53.8 million of its sewer revenue bonds that is expected to decrease future aggregate debt service payments by $7.2 million over the life of the bonds.

As of December 31, 2004, the County has two short-term limited tax general obligation bond anticipation notes outstanding of $46.4 million that will mature on November 1, 2005. The Notes were issued to finance the County Courthouse seismic project, other building construction and improvement projects, and Open Space Acquisitions Projects. The County paid and retired 2003A Notes of $80.0 million on October 1, 2004, with proceeds from the issuance of $82.4 million of limited tax general obligation bonds.

The County maintains a rating of "Aa1" from Moody's and "AA+" from Standard & Poor's for its limited tax general obligation debt and a rating of "Aaa" from Moody's and "AA+" from Standard & Poor's for its unlimited tax general obligation debt. The ratings are "A1" from Moody's and "AA-" from Standard & Poor's for its Wastewater Treatment Division's revenue debt.

State statutes limit the amount of general obligation debt the County may issue to 2½ percent of its total assessed valuation for both general county purposes and for metropolitan functions. The current debt limitation of total general obligations is $6,222.8 million for both general county purposes and for metropolitan functions, which is significantly higher than the County's outstanding general obligation debt of $1,291.4 million for general county purposes and $555.3 million for metropolitan functions.

During the first quarter of 2005 the County completed the sale of $200.0 million of limited tax general obligation bonds payable from Sewer Revenues to finance its Wastewater capital improvement program. These bonds are additionally secured by a pledge of the revenues of the County's sewer system.

Additional information on King County's long-term debt can be found in this report in Note 13 – Debt.

ECONOMIC FACTORS, INITIATIVES, AND NEXT YEAR'S BUDGETS AND RATES

- Property value growth remained relatively slow in 2004, with assessed valuation up 5.5 percent, compared with 4.8 percent growth in 2003, 6.6 percent growth in 2002, 12.0 percent growth in 2001 and 13.3 percent growth in 2000. The ailing commercial market has stabilized, but positive valuation growth is almost entirely attributable to robust demand for residential property. Housing has been buoyed in large measure by historically low interest rates.

  Washington State Initiative Measure No. 747 (I-747) was approved by the voters in November 2001. I-747 reduced the limit on the total dollar amount of regular property taxes that may be levied annually by a taxing district (including the County) without a vote of its electors from 106 percent to 101 percent of the highest levy in the three previous years, excluding new construction, improvements, and state-assessed property. Because I-747's limitation applies to the dollar amount levied rather than to levy rates, increases in the value of existing property exceeding one percent per year will result in decreasing tax levy rates.

- For the first time in four years, General Fund retail sales tax revenues in the County increased, up 6.16 percent in 2004, a sharp turnaround from the 0.72 percent decline in 2003. Between 2001 and 2003 General Fund sales tax revenues declined by 7.2 percent; the decline of 3.5 percent in 2001 was the first since the institution of the local option sales tax in 1971.

- Employment in King County was once again on the rise after more than two years of recession and job losses. The annual average unemployment rate in King County in 2004 was 5.1 percent as compared to 6.8 percent in 2003. While indications of a modest recovery are encouraging, the Countywide Planning Policies are also addressing the issues of income disparity, living wage, and poverty.

- In 2004 there were no large annexations or incorporations. Census data in 2000 confirmed the continued decline in the County's unincorporated area population while overall County population grew. Between 1990 and 2000, the county's population grew from 1.5 million to 1.7 million. In 1990 more than 500,000 people lived in unincorporated King County; by 2000, this had declined to 350,000. The fiscal impacts of annexation and incorporation on the County depend on the revenue-generating capacity of an area compared with its service demands. Many of the remaining unincorporated urban areas of the County do not generate significant commercial activity and sales tax revenues, although these areas have relatively high service demands. The taxpayers of the region subsidize services provided to these urban unincorporated areas.

  As part of the 2004 Adopted Budget, the County began a multi-year initiative promoting the accelerated annexation of the remaining urban areas in unincorporated King County. The Annexation Initiative reflects a substantial commitment to the implementation of the State Growth Management Act and the Countywide Planning Policies. In addition, the success of the Annexation Initiative will likely generate considerable expenditure savings for the General Fund as the accelerated annexations and possible incorporations occur. In 2005 the Annexation Initiative will continue to actively pursue annexations of ten major urban unincorporated areas with significant service obligations. If all ten of the major urban unincorporated areas are annexed, incorporated, or some combination thereof, the potential benefit is conservatively estimated to be as high as $13.6 million annually.

- King County remains a leader in regional transportation. All three of the County's major transportation assets, Metro Transit, Road Services and the King County International Airport, are facing financial challenges. Metro Transit is heavily dependent on sales tax revenue which has been weakened by the recession. This revenue shortfall, combined with higher than anticipated diesel fuel costs, allows for only limited new bus service hour additions over the next six years. A modest fare increase for 2005 was proposed, but was rejected by the King County Council. However, increases in operating costs will eventually require some increases in fares in the near future.

  The loss of the local option vehicle license fee (VLF) revenues (as a result of State Initiative Measure No. 776 (I-776), approved by voters in November 2003) had a substantial impact on the County's six-year Roads capital improvement programs in 2004. The County was forced to eliminate almost $80 million of essential road improvements over the next six years as a result of the loss of this revenue source. The need for critical road and bridge improvements remain a priority while the County continues its efforts to identify funding to increase the capacity of our road system.

  The Puget Sound Regional Transportation Investment District (RTID) — consisting of King, Pierce and Snohomish counties — was created in March 2002, when the State Legislature approved a measure that allows regions within the state to work together to solve their own transportation problems through local funding. The RTID legislation allows for a mix of funding sources. The RTID Executive Board is currently considering a combination of local sales tax, vehicle licensing fees, and vehicle excise taxes. The board is also considering tolls on major roads in King County and a regional gas tax.

The King County International Airport is facing several budget challenges as revenues are not keeping pace with expenses. In the 2005 budget, a combination of fee increases and cuts in expenses were used to balance the airport financial plan. The County will continue to explore ways to assure the continued safe operation of the airport as a self-sufficient regional economic asset.

- By law, the County is required to adopt a balanced budget. The entire 2005 budget for the County, adopted by the County Council in November 2004, totals $3,413.7 million. Of this amount, $562.1 million is appropriated for the General Fund; $690.0 million for enterprise funds (including public transportation, solid waste and wastewater treatment); and $703.5 million for special revenue funds (including public health, emergency medical services, human services, and road funds). The budget also includes $374.4 million committed to capital improvements for roads, parks, and other major public facilities.

  The structural deficit in the General Fund budget continues to persist due primarily to the constraints on property tax growth as a result of passage of I-747, growing demands on the criminal justice system, and a 150-year-old archaic funding structure under which counties in the State of Washington struggle.

- Two key priorities in 2005 are: 1) a transformation in the delivery of human services with the objective of ending homelessness. King County is the second largest provider of human services in the state. The County Executive's Task Force on Regional Human Services called for creation of a more stable human services system. The task of building a stable revenue plan and a community to deliver the services is a key focus of this budget. In addition, King County will become the regional coordinator of the Committee to End Homelessness; and 2) an innovative approach in the delivery of criminal justice services through partnerships that stabilize the lives of offenders through stable housing, appropriate treatment, education and employment aimed at breaking the cycle of crime, restoring productive citizens, and reducing the jail population while continuing to keep our communities safe.

- Since 2000 the Washington State Legislature has acted repeatedly to change the underlying economic assumptions for State pension plans, effectively reducing State and local government contribution levels. Employer contribution rates, and the cost to King County, are projected to increase substantially over the next several years to bring the contribution rates up to actuarially sound levels.

REQUESTS FOR INFORMATION

This financial report is designed to provide an overview of the County's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to the Chief Accountant/Manager, Financial Management Section, Room 653 Administration Building, 500 Fourth Ave., Seattle, WA 98104.

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