CAFR

Financial Section

Washington State Auditor
Brian Sonntag

INDEPENDENT AUDITOR'S REPORT

July 14, 2008

County Council and 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, 2007, which collectively comprise the County's basic financial statements, 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 Harborview Medical Center, which statements reflect 60 percent, 59 percent, and 97 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 report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for Harborview Medical Center, is based solely on the report 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 report of the other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the report of the 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, 2007, and the respective changes in financial position and, where applicable, cash flows thereof, and the respective budgetary comparison for the General Fund and Public Health Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

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As described in Note 1, during the year ended December 31, 2007, the County has implemented the Governmental Accounting Standards Board's Statement 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions.

The management's discussion and analysis on pages 3 through 19 and 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 the County's basic financial statements. The accompanying information listed as combining and individual fund statements and schedules and supplementary information on pages 127 through 228 is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has 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 report of the other auditors, is 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 County. 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, 2007. 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, 2007, the assets of the County exceeded its liabilities by $3,923.2 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 $204.0 million deficit at the end of the year.
- In 2007 the County's total net assets increased by 7.9 percent or $286.6 million. The governmental net assets increased by 11.3 percent or $182.6 million, and the business-type net assets increased by 5.1 percent or $104.0 million.
- As of December 31, 2007, the County's governmental funds reported combined ending fund balances of $472.0 million. Approximately 72.8 percent or $343.6 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 2007 the unreserved, undesignated fund balance for the General Fund was $90.0 million, amounting to 15.8 percent of total General Fund expenditures for 2007. Total fund balance for the General Fund decreased 2.2 percent or $3.1 million for the year.
- The County's total bonded debt increased by 5.4 percent or $186.9 million in 2007 due to new bond issuance of $339.0 million offset by $145.7 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 2007 operations of the County's four flood control zone districts. 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. Beginning in 2007, four Washington state nonprofit corporations, each of which are single-purpose entities that were created to assist the County in the development and construction of public buildings, are reported as blended component units of the County. A single internal service fund, the Building Development and Management Corporations Fund, is used to blend the four nonprofit corporations' activities and balances with the primary government.

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 five 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), the Cultural Development Authority (CDA) of King County, doing business as 4Culture, Flood Control Zone Districts, and four Washington state nonprofit corporations each of which are single-purpose entities that were created to assist the County in the development and construction of public buildings. Financial information for the first three of 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 the HMC, the PFD, and the CDA 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 how cash and other financial assets can readily be converted to available resources, and the balances left at year-end that are available for future 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). Two governmental funds, the General Fund and the Public Health 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 each of the two major governmental funds.

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, building development and construction, 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.

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.

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 $3,923.2 million at the end of 2007. This is an increase of 7.9 percent or $286.6 million over the net assets of the previous year, as restated.

Governmental activities. Although net assets of the County's governmental activities increased 11.3 percent to $1,799.2 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 $357.9 million deficit at the end of 2007. This is a 1.7 percent or $6.2 million decrease in the deficit in unrestricted net assets from that of fiscal year-end 2006, as restated.

Net Assets
(in thousands)

	Governmental Activities		Business-type Activities		Total	
	2007	2006	2007	2006	2007	2006
Assets						
Current and other assets	$ 1,080,590	$ 972,446	$ 951,698	$ 825,714	$ 2,032,288	$ 1,798,160
Capital assets	2,416,437	2,248,667	4,123,272	3,805,845	6,539,709	6,054,512
Total Assets	3,497,027	3,221,113	5,074,970	4,631,559	8,571,997	7,852,672
Liabilities						
Long-term liabilities	1,475,758	1,314,783	2,658,464	2,382,170	4,134,222	3,696,953
Other liabilities	222,119	289,776	292,423	229,335	514,542	519,111
Total Liabilities	1,697,877	1,604,559	2,950,887	2,611,505	4,648,764	4,216,064
Net Assets						
Invested in capital assets, net of related debt	1,762,158	1,642,456	1,551,017	1,566,302	3,313,175	3,208,758
Restricted	394,932	338,188	419,118	329,262	814,050	667,450
Unrestricted	(357,940)	(364,090)	153,948	124,490	(203,992)	(239,600)
Total net assets	$ 1,799,150	$ 1,616,554	$ 2,124,083	$ 2,020,054	$ 3,923,233	$ 3,636,608

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 2007 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 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 $461.8 million, $61.4 million less than at the end of 2006, for which no corresponding assets are recorded but for which future revenues are obligated.

Of the amount of debt with no corresponding assets, 71.8 percent or $331.7 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 ($136.0 million), and the Harborview Medical Center ($195.7 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 $98.7 million associated with the Kingdome facility, which was demolished to make room for the Seahawks (Qwest) Football Stadium, and $31.4 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 5.1 percent to $2,124.0 million in the net assets of business-type activities. Of the total net assets for business-type activities, 73.0 percent or $1,551.0 million is invested in capital assets (e.g., land, buildings, vehicles, plant assets, equipment, and work in progress), net of related debt. 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 19.7 percent of the total net assets of business-type activities is restricted as to use for capital construction ($370.6 million), debt service ($43.4 million), and litigation ($5.1 million). The remaining 7.3 percent or $153.9 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 $357.9 million deficit in the governmental activities unrestricted net assets and the $153.9 million positive balance in the business-type activities unrestricted net assets resulted in the deficit of $204.0 million in total unrestricted net assets for the County as a whole.

Analysis of Changes in Net Assets

The increase in the County's total net assets in 2007 resulted from revenues exceeding related expenses and reflects the County's ability to meet its ongoing obligations including its debt service requirements. Approximately 44.4 percent of the County's total revenues came from taxes, primarily Property taxes and the Retail sales and use taxes. Charges for various goods and services provided 40.7 percent of the total revenues, while 12.7 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 2007 fiscal year.

Governmental activities. Governmental activities accounted for 63.7 percent of the total growth in net assets of the County, resulting in an increase in the County's governmental activities net assets of $182.6 million. Program revenues for governmental activities total $802.3 million and include the amount paid by those who directly benefited from the programs ($539.2 million), and by other governments and organizations that subsidized certain programs with operating grants and contributions ($180.2 million), and capital grants and contributions ($82.9 million). In 2007 the cost of all governmental activities was $1,390.7 million. The County paid for the $588.5 million remaining "public benefit" portion of governmental activities with $499.3 million in property taxes, $164.8 million in retail sales and use taxes, and $105.7 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.

The growth in net assets of governmental activities of $182.6 million is primarily due to the following factors: the collection of revenues (mostly taxes) to fund repayments of long-term debt ($87.2 million), the collection of revenues for the acquisition of capital assets ($25.7 million), donations of capital assets (primarily infrastructure) to the county ($57.8 million), taxes collected by Special Revenue Funds (Automated Fingerprint Identification System Fund and Veterans and Human Services Fund) in excess of the services provided in 2007 ($16.2 million). In addition, book value of capital assets sold/retired ($18.1 million) and depreciation expense ($27.3 million) were negative factors in the change in net assets.

Changes in Net Assets
(in thousands)

	Governmental Activities		Business-type Activities		Total	
	2007	2006	2007	2006	2007	2006
Revenues						
Program revenues						
Charges for services	$ 539,165	$ 487,479	$ 538,791	$ 500,165	$ 1,077,956	$ 987,644
Operating grants and contributions	180,215	183,563	55,771	56,400	235,986	239,963
Capital grants and contributions	82,908	101,861	15,846	37,366	98,754	139,227
General revenues						
Property taxes	499,339	468,740	-	-	499,339	468,740
Retail sales and use taxes	164,804	150,111	442,042	367,264	606,846	517,375
Other taxes	69,356	72,123	-	-	69,356	72,123
Unrestricted interest earnings	36,348	46,009	22,718	28,833	59,066	74,842
Total revenues	1,572,135	1,509,886	1,075,168	990,028	2,647,303	2,499,914
Expenses [a]						
General government [b]	95,864	88,278	-	-	95,864	88,278
Law, safety and justice	544,838	509,234	-	-	544,838	509,234
Physical environment	63,326	56,322	-	-	63,326	56,322
Transportation	107,471	96,401	-	-	107,471	96,401
Economic environment	94,555	92,460	-	-	94,555	92,460
Mental and physical health	381,286	361,817	-	-	381,286	361,817
Culture and recreation	50,100	40,974	-	-	50,100	40,974
Interest and other debt service costs	53,299	52,361	-	-	53,299	52,361
Airport	-	-	14,620	15,392	14,620	15,392
Public transportation	-	-	588,234	535,471	588,234	535,471
Solid waste	-	-	116,252	102,127	116,252	102,127
Water quality	-	-	242,808	243,496	242,808	243,496
Other enterprises activity	-	-	8,025	6,687	8,025	6,687
Total expenses	1,390,739	1,297,847	969,939	903,173	2,360,678	2,201,020
Increase in net assets before transfers	181,396	212,039	105,229	86,855	286,625	298,894
Transfers	1,200	(2,531)	(1,200)	2,531	-	-
Increase in net assets	182,596	209,508	104,029	89,386	286,625	298,894
Net assets, beginning of year (restated) [c]	1,616,554	1,407,046	2,020,054	1,930,668	3,636,608	3,337,714
Net assets, end of year	$ 1,799,150	$ 1,616,554	$ 2,124,083	$ 2,020,054	$ 3,923,233	$ 3,636,608

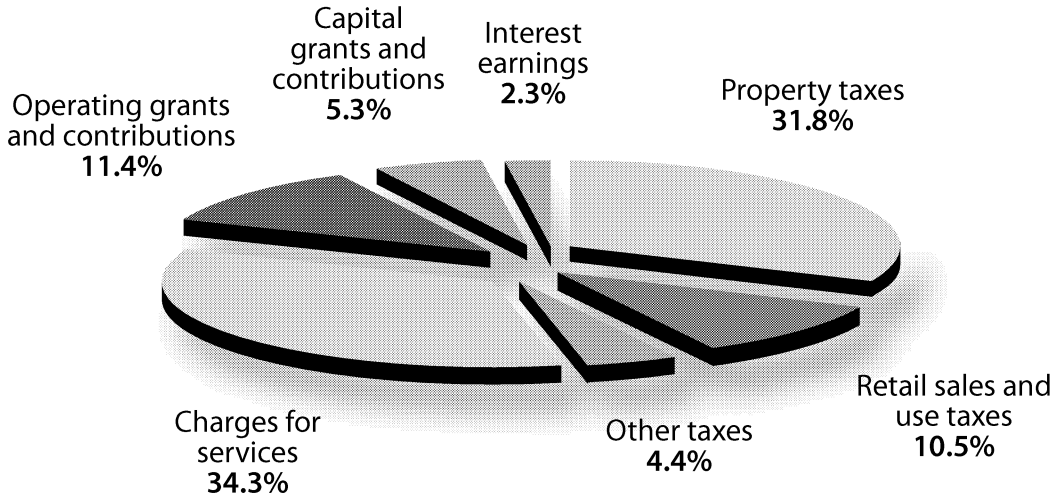
(a) Expenses for all functions include the allocation of indirect expenses from the general government function. The amount of indirect general government expenses allocated to each function is shown in a separate column on the County's government-wide Statement of Activities alongside the column that reflects the direct operating expenses incurred by each function. As a result of this allocation, the $95.9 million in General government expense above consists of $147.7 million in direct program expenses and loss on disposal (transfer) of capital assets of $12.6 million reduced by a net allocation of $64.4 million to other County functions.

(b) General government expenses includes loss on sale/disposal of capital assets of $12.6 million and $22.3 million in 2007 and 2006, respectively.

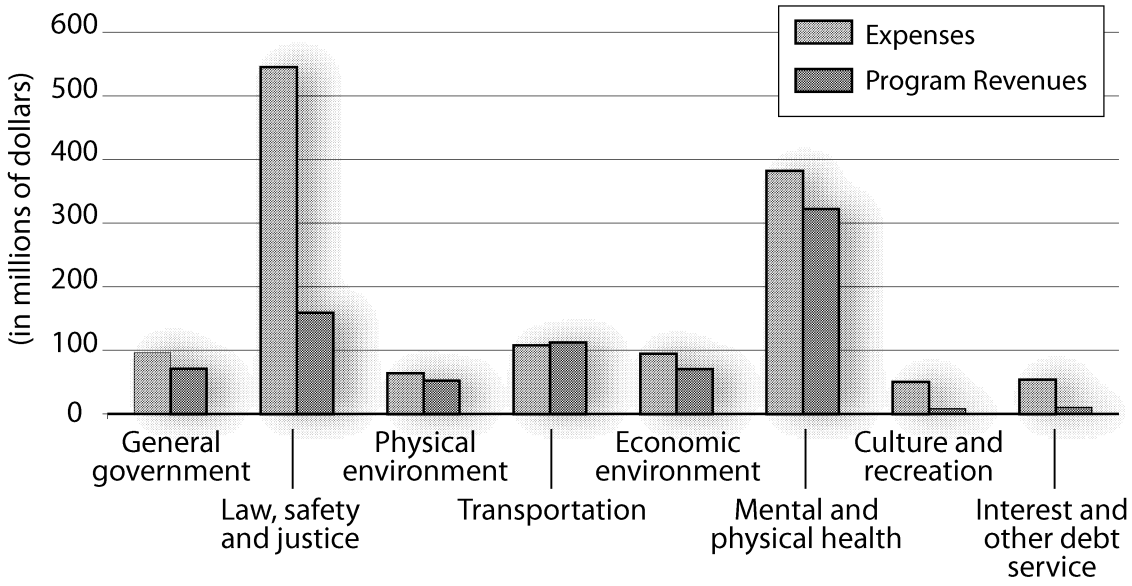
(c) Net assets, beginning of year has been restated, see Note 15, "Restrictions, Reserves, Designations, and Changes in Equity" – Restatements of Beginning Balances.

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
2007



Expenses and Program Revenues — Governmental Activities
2007



Charges for services provided 34.3 percent, and property taxes 31.8 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 84.4 percent of the activities for that function. In 2007 Transportation received $57.0 million in infrastructure and right-of-way capital assets from developers, which enabled program revenues to exceed expenses. These capital contributions accounted for nearly one-third of the 2007 increase in governmental activities net assets.

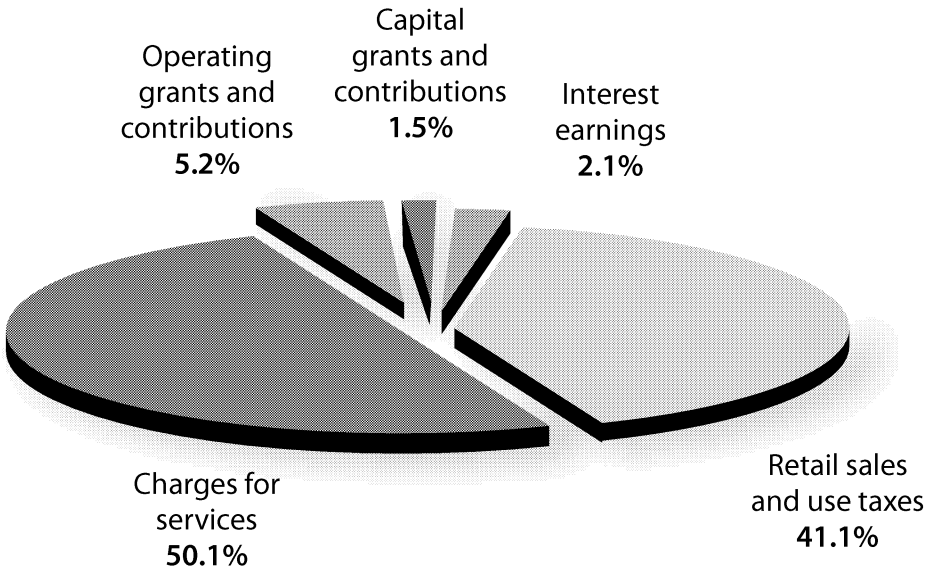
A comparison of the cost of services by function for the County's governmental activities is shown below, along with the revenues used to cover the net expenses of the governmental activities (in thousands):

(Expenses) Net of Program Revenues	
General government	$ (25,404)
Law, safety and justice	(386,060)
Physical environment	(11,323)
Transportation	4,035
Economic environment	(24,334)
Mental and physical health	(59,525)
Culture and recreation	(42,139)
Interest and other debt service costs	(43,701)
Total expenses	(588,451)
General revenues	
Property taxes	499,339
Retail sales and use taxes	164,804
Other taxes	69,356
Unrestricted interest earnings	36,348
Other	1,200
Increase in net assets	$ 182,596

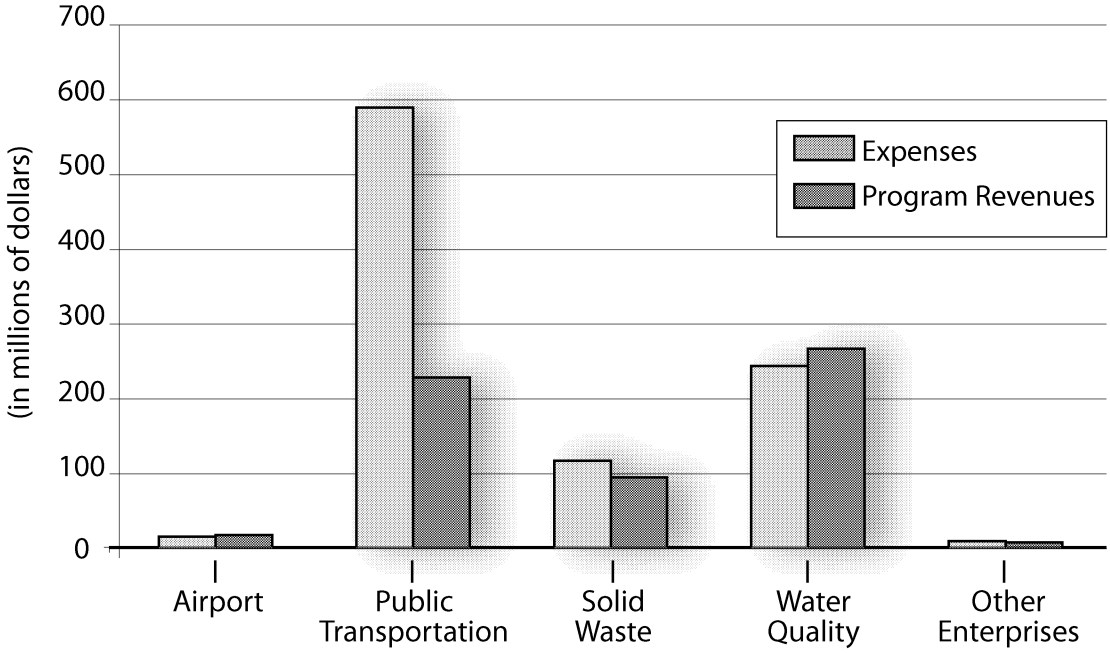
Business-type activities. Business-type activities increased the County's net assets by $104.0 million in 2007, accounting for 36.3 percent of the total growth in net assets of the County. Total revenues for business-type activities were $1,075.1 million. The cost of all business-type activities for 2007 was $969.9 million. Of that amount, 62.9 percent or $610.4 million was funded from program revenues, including $538.8 million in charges for services, $55.8 million from other governments and organizations that subsidized certain programs with operating grants, and $15.8 million in capital grants and contributions. The Public Transportation program operations are subsidized with retail sales and use tax revenues, which amounted to $442.0 million in 2007. In addition, business-type activities earned $22.7 million in unrestricted interest earnings.

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 2007



Expenses and Program Revenues — Business-type Activities 2007



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 balances may serve as a useful measure of a government's net financial resources available for spending at the end of the fiscal year.

As of December 31, 2007, the County's governmental funds reported combined ending fund balances of $472.0 million, an increase of $51.6 million in comparison with the prior year. Approximately 72.8 percent ($343.6 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 ($83.3 million), to pay debt service ($17.6 million), for prepayments ($5.8 million), and for a variety of other restricted purposes ($21.7 million).

Overall governmental fund revenues totaled approximately $1,558.0 million for 2007, which represents an increase of 5.1 percent, or $75.4 million, over the fiscal year ended December 31, 2006. The increase was primarily due to strong growth in Property taxes (up $30.6 million), Retail sales and use taxes (up $14.7 million), Intergovernmental revenues (up $11.5 million), and Charges for services (up $16.2 million). Interest earnings were down $9.0 million due to unrealized losses on impaired investments. In 2007, expenditures for governmental funds totaled $1,563.8 million, an increase of 5.0 percent or $74.4 million from the previous fiscal year. Current expenditures were up 8.1 percent or $100.7 million from the previous fiscal year, Debt service expenditures (excluding the payment to escrow agent) were down $7.7 million (5.6 percent), and Capital outlay expenditures were down $12.6 million (14.5 percent). Total expenditures for governmental funds exceeded revenues by $5.8 million in 2007 compared to $6.8 million for the 2006 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 $140.6 million. Unreserved fund balance, the amount considered available to spend, totaled $113.3 million. Of that amount, $23.3 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 19.9 percent of total General Fund expenditures, a decrease from the 22.5 percent of a year ago. Total fund balance represents 24.7 percent of total General Fund expenditures, a decrease from the 27.1 percent of a year ago.

The fund balance of the County's General Fund decreased by $3.1 million during 2007, while the fund balance decrease in 2006 was a modest $227 thousand. While revenues were up $33.5 million (5.6 percent) in 2007, expenditures were up $37.6 million (7.1 percent) and Other Financing Uses were down $851 thousand. The $33.5 million increase in revenues includes an increase of $22.4 million in Taxes, $3.3 million in Intergovernmental revenues, and $8.5 million in charges for service. Interest earning declined $5.5 million in 2007 due to unrealized losses on impaired investments. The total $36.7 million (6.1 percent) net increase in expenditures and other financing uses reflect the increased support for programs and services. Over $24.9 million of the $37.6 million increase in expenditures was in the Law, Safety, and Justice function,

including increased expenditures of $3.7 million for Adult and Juvenile Detention (up 6.8 percent), $7.1 million in the Sheriff's Office (up 6.1 percent), $2.7 million in the Office of the Prosecuting Attorney (up 5.2 percent), and $5.3 million in increased expenditures for the courts (up 6.6 percent). Other significant increases in current expenditure functions in 2007 include $9.6 million in general government and $1.2 million in economic environment.

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 2007 it had a total fund balance of $6.4 million (down from $7.7 million at the end of 2006), of which $5.6 million was unreserved and available for spending. The $9.0 million decrease in revenues from the 2006 level is due to a $10.7 million decrease in Intergovernmental revenues. Other revenues were up $1.7 million. In 2007, expenditures decreased by $2.6 million.

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 previously discussed in the business-type activities, the County's net assets increased by $104.0 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 $87.6 million of this increase while the net assets of the Water Quality Enterprise increased by $29.2 million. In 2007, net assets of the Solid Waste Enterprise declined by $19.4 million. On July 9, 2007, the King County Council adopted an increase in the Solid Waste Tipping Fee from $82.50 to $95.00 per ton, effective January 1, 2008, to ensure the financial stability of the enterprise.

The **Public Transportation Enterprise** accounts for the operations, maintenance, capital improvements, and expansion of public transportation and related facilities in the County. At the end of 2007 the Public Transportation Enterprise had total net assets of $1,376.9 million of which 71.7 percent or $986.6 million was invested in capital assets, net of related debt; 22.5 percent or $309.6 million was restricted as to use for capital purposes and bond reserves; and 5.8 percent or $80.7 million was unrestricted and available for spending. Net assets of Metro Transit increased in years 2007 and 2006. The increase was $87.6 million (6.8 percent) in 2007 and $48.6 million (3.9 percent) in 2006. The change in 2007 is attributed to an increase in cash balances held for future fleet replacement and future capital investments that are currently projected to occur over the next few years. During 2007, Metro Transit benefited from both strong sales tax growth and the additional 0.1 percent of sales tax levied beginning April 1, 2007. Compared with 2006, sales tax grew 20.4 percent or $74.8 million from the 2006 levels. The reserve for future fleet replacement continued to be replenished consistent with existing policies and in anticipation of upcoming fleet replacements over the next several years.

The **Water Quality Enterprise** accounts for the operations, maintenance, capital improvements, and expansion of the County's water pollution control facilities. Total net assets in the Water Quality Enterprise were $538.7 million at the end of 2007 of which 72.3 percent or $389.4 million was invested in capital assets, net of related debt; 18.0 percent or $97.2 million was restricted as to use for construction projects, debt service, and litigation; and the remaining 9.7 percent or $52.1 million was unrestricted and available for spending. Water Quality operating revenues increased by 9.0 percent in 2007 to $262.9 million, while operating expenses net of depreciation increased $4.5 million to $95.6 million. This compares to operating revenues increased by 9.2 percent in 2006 to $241.3 million and operating expenses net of depreciation increased by $7.5 million to $91.1 million. The monthly sewer rate increased to $27.95 per

Residential Customer Equivalents (RCE) in 2007 from $25.60 in 2006, while the capacity charge rate grew to $42.00 per RCE in 2007 from $34.05 in 2006. Rates did not increase in 2006. Capacity charge revenues increased $4.9 million or 22.0 percent in 2007, and $5.2 million or 30.7 percent in 2006. Total sewer customers billed for sewer treatment services increased by 12,012 to 702,946 in 2007, and 1,117 to 690,934 in 2006.

General Fund Budgetary Highlights

The County's final General Fund budget differs from the original budget in that it reflects an increase in appropriations of $24.3 million during the year due to 2007 supplemental budget appropriations for General Fund support for children and family services, public health, and capital projects. However, actual budgetary basis expenditures were only $8.3 million more than the original budget. This resulted in an underutilization of the total final appropriation authority by $16.0 million, including $4.4 million underexpenditures in General governmental services; $3.4 million in Law, safety and justice; and $5.8 million in Transfers out. During the year total revenues exceeded budgetary estimates by $12.4 million with a net impact of reducing the fund balance by $3.1 million in 2007.

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, 2007, amounts to $6.5 billion (net of accumulated depreciation). Capital assets include land, right-of-way, conservation easements and development rights, buildings, improvements other than buildings, roads and bridges infrastructure, vehicles, machinery, computers and other equipment, and construction work-in-progress. The total increase in the investment in capital assets over the previous year was 8.0 percent (7.5 percent increase for governmental activities and 8.3 percent increase for business-type activities).

Major capital asset events during 2007 included the following:

- Construction of the Brightwater treatment system went on its second full year in 2007. This project comprised the bulk of the 43.3 percent increase in business-type work in progress during the year. Construction activities are simultaneously ongoing in the treatment plant, the conveyance systems (portals and conveyance pipes), and ancillary facilities. Construction is expected to be completed in 2010, with operations starting in 2011.

- Significant construction activity is also noted in the Public Transportation and Solid Waste enterprises. Public transportation continued to do improvements, additions, or remodels of bus bases, transit centers, and park-and-ride facilities. The joint project of retrofitting the Seattle Transit Tunnel to accommodate light rail was completed in 2007. For the Solid Waste Enterprise improvements to existing transfer stations and development of landfill ancillary systems continued.

- For governmental activities, the County acquired a new office building and detached parking garage at a combined cost of $97.2 million which was financed and developed by a non-profit corporation using "63-20" financing. The building is used by various administrative offices of the County who previously leased space in other private and public buildings. Another similarly financed building is currently under construction which will house the Medical Examiner's facilities. Security system upgrades to the King County Correctional Facility (in Seattle) were completed in 2007 and other planned improvements to jail operations were underway.

A summary of the 2007 capital assets activity is shown below (in millions). The restatements of 2006 balances for infrastructure and right-of-way were due to reclassifications of previously capitalized costs to preservation and maintenance and other miscellaneous adjustments. The restatements of 2006 balances in buildings were due to cost basis adjustments that resulted from the change in accounting for certain governmental buildings previously accounted for as capital leases but now recognized as County-owned. More detailed information on the County's capital assets can be found in Note 6 – Capital Assets.

	Governmental Activities			Business-type Activities		Total	
	2007	2006		2007	2006	2007	2006
Land	$ 735.9	$ 716.7	**	$ 332.0	$ 324.8	$ 1,067.9	$ 1,041.5
Buildings*	540.8	437.0	**	679.9	691.8	1,220.7	1,128.8
Improvements other than buildings*	16.5	17.7		1,260.2	1,296.7	1,276.7	1,314.4
Infrastructure	927.9	866.9	**	-	-	927.9	866.9
Equipment*	79.7	75.8		480.9	536.5	560.6	612.3
Construction in progress	115.6	134.6	**	1,370.3	956.1	1,485.9	1,090.7
Total	$ 2,416.4	$ 2,248.7		$ 4,123.3	$ 3,805.9	$ 6,539.7	$ 6,054.6

* Net of depreciation

** Restated

Infrastructure

The County has elected to use the modified approach in reporting 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 Services Division to maintain at least 80.0 percent of the road system at a PCI of 40 or better. In the most recent condition assessments, 91.1 percent of the arterial roads in the County and 89.1 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 2007 for road preservation and maintenance was $61.9 million. The amount actually expended was $51.8 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. Trend analysis of preservation and maintenance should consider the prior period adjustments that were made for 2003-2006 as shown in the RSI section, p. 124.

The County currently maintains 184 bridges. Physical inspections to uncover deficiencies are carried out at least every two years and documented. There is also an annual evaluation to determine which bridges are due 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 Services Division is to maintain bridges in such a manner that no more than 12 (6.5 percent) will have a sufficiency rating of 20 or less. The most current complete assessment showed 6 bridges at or below this threshold. The amount budgeted in 2007 for bridge preservation and maintenance was $24.8 million. Actual amount expended was $16.2 million. Underspending of the budgeted amount is due to the construction schedule of certain projects extending beyond the budget year. Trend analysis of preservation and maintenance should consider the prior period adjustments that were made for 2003-2006 as shown in the RSI section, p. 125.

Debt Administration

At the end of 2007, King County Primary Government has total bonded debt outstanding of $3,621.3 million for its governmental and business-type activities. Of this amount, $1,897.1 million is comprised of debt backed by the full faith and credit of the County. The $1,724.2 million remainder of the County's bonded debt represents bonds secured solely by specified revenue sources (revenue bonds).

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

	Governmental Activities		Business-type Activities		Total	
	2007	2006	2007	2006	2007	2006
General obligation bonds	$ 819.2	$ 870.4	$ 663.4	$ 642.4	$ 1,482.6	$ 1,512.8
General obligation lease revenue bonds	414.5	422.5 [(a)]	-	-	414.5	422.5
Revenue bonds	-	-	1,724.2	1,499.1	1,724.2	1,499.1
Total	$ 1,233.7	$ 1,292.9	$ 2,387.6	$ 2,141.5	$ 3,621.3	$ 3,434.4

(a) Restated to reclass Issaquah District Court as capital leases and to include Goat Hill Properties and NJB Properties lease revenue bonds, issued in 2005 and 2006 respectively. See Note 13, "Debt " – Schedule of Long-term debt.

The total bonded debt was increased over 2006 by 5.4 percent or $186.9 million (4.6 percent or $59.2 million decrease for governmental activities and 11.5 percent or $246.1 million increase for business-type activities). The decrease of bonded debt outstanding in the governmental activities was primarily due to the $90.1 million of debt service payments in 2007. The business-type activities' bonded debt was increased due to the issuance of $250.0 million of sewer revenue bonds to finance the capital needs of the Water Quality Enterprise and $40.6 million for Solid Waste Division's capital improvement program.

During 2007 the County refinanced some of its existing debt through advance refunding to take advantage of favorable interest rates:

- The County refinanced $56.3 million of general obligation bonds that is expected to decrease future aggregate debt service payments by $5.8 million over the life of the bonds.

- The County also refinanced $66.1 million of lease revenue bonds that is expected to decrease future aggregate debt service payments by $4.8 million over the life of the bonds.

- Using excess proceeds from special taxes and revenues, the County completed a partial defeasance of general obligation (baseball stadium) bonds that is expected to decrease debt service payments by $13.9 million.

The County maintains a rating of "Aa1" from Moody's, a rating of "AAA" from Standard & Poor's, and a rating of "AA+" from Fitch for its limited tax general obligation debt. For its unlimited tax general obligation debt, the County has a rating of "Aaa" from Moody's, a rating of "AAA" from Standard & Poor's, and a rating of "AAA" from Fitch. The ratings for its Water Quality Enterprise's revenue debt are "A1" from Moody's and "AA" from Standard & Poor's.

State statutes limit the amount of general obligation debt that the County may issue to 2 ½ percent of its total assessed valuation for both general county purposes and metropolitan functions. The current debt limitation of total general obligations is $8,524.9 million for both general county purposes and metropolitan functions, which is significantly higher than the County's outstanding net general obligation long-term liabilities of $1,321.5 million for general county purposes and $697.9 million for metropolitan functions.

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

ECONOMIC OUTLOOK AND NEXT YEAR'S BUDGET

Economic factors have a direct impact on the County's revenues and the demand for services. The County's revenue sources include taxes, charges for services, and intergovernmental revenues. The largest single source is taxes, which comprise approximately forty percent of total revenues and consist primarily of taxes on real property and retail sales and use taxes. Property taxes tend to be stable because levy rates are calculated months in advance and King County establishes assessed value from the preceding four years of real estate sales. Other tax sources, such as retail sales tax, are more volatile and directly influenced by economic conditions in the region.

Property assessed valuation increased by 14.2 percent and 10.5 percent in 2007 and 2006, respectively. Property tax collections grew by 4.2 percent in 2007 compared with 2.5 percent growth in 2006. Total regional employment growth and regional population growth are expected to be 1.8 percent. Unemployment in King County was 3.7 percent in 2007 compared with 4.1 percent in 2006. Personal income has grown by 8.0 percent on average between 2005 and 2007. These and other factors were considered in the budget enacted for 2008. By law, the County is required to adopt a balanced budget. The 2008 budget for the County, adopted by the County Council in November 2007, totals $4,398.9 million. Of this amount, $687.2 million is appropriated for the General Fund; $987.0 million for enterprise funds (including public transportation, solid waste and wastewater treatment); and $885.9 million for special revenue funds (including public health, emergency medical services, human services, and road funds). The budget also includes $1.2 billion committed to capital improvements for wastewater treatment, transit, roads, parks and other major public facilities. The general fund current expense budget maintained a six percent budgetary undesignated fund balance as a percentage of revenues.

Other considerations

King County will continue to face numerous challenges including volatile energy prices, rising employee and programmatic healthcare costs, the cost of providing services to urban unincorporated areas, and the need to raise sufficient revenues to support utility, transit system

and general government activities. The County projects structural deficits for the General Fund budget occurring in years 2009 through 2012.

The County investment pool held four impaired commercial paper investments at December 31, 2007. The county pool is a senior creditor for each investment, and each investment is part of an enforcement event in which a trustee takes over the administration of the program and determines the best way to liquidate assets or restructure the portfolio. Enforcement events are designed to protect the interests of senior creditors. The maximum risk of loss on the four investments is $207 million at December 31, 2007; and has been reduced to $190 million by payments received during 2008. An $83.3 million unrealized loss was recorded at December 31, 2007. The ultimate outcome on the investments will be determined based upon results of the enforcement events.

Property tax is the largest revenue source in the County general fund at 40 percent of total general fund revenues. The council-approved property tax levy is limited to one percent growth each year plus the property tax on new construction.

The County is in the fifth year of an annexation initiative and will face operational and budgetary adjustments as annexations are completed. Ten major urban unincorporated areas are identified that by County Planning Policies should be incorporated into or annexed into cities by 2012. Incorporation or annexation is also encouraged by the Washington State Growth Management Act. Major annexation areas are in various stages of the annexation process. In 2007, there were two large annexations approved: the City of Auburn annexed the Lea Hill area with an effective date of January 1, 2008, and assessed valuation of $815.8 million and the City of Renton annexed the Benson Hill area with an effective date of March 1, 2008, and assessed valuation of $1.2 billion. The completion dates of other major annexations are not currently known. The fiscal impacts of incorporation and annexation depend upon the revenue generating capacity of an area compared to its service demands. The 2008 adopted budget made a policy reserve of $7.8 million for annexation incentives.

In early 2006, the Washington State Legislature enacted a credit against the state sales tax for cities that annex areas with over ten thousand residents. The annexing city is eligible for the credit, which is effectively a sales tax rate of 0.1 percent, applied to the newly annexed area and within the prior city. If the annexed area population exceeds twenty thousand, the applicable credit is 0.2 percent. Annexing cities must complete annexations by January 1, 2010 to be eligible for the credit.

REQUESTS FOR INFORMATION

This financial report is designed to provide an overview of the County's financial activities 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.

King County