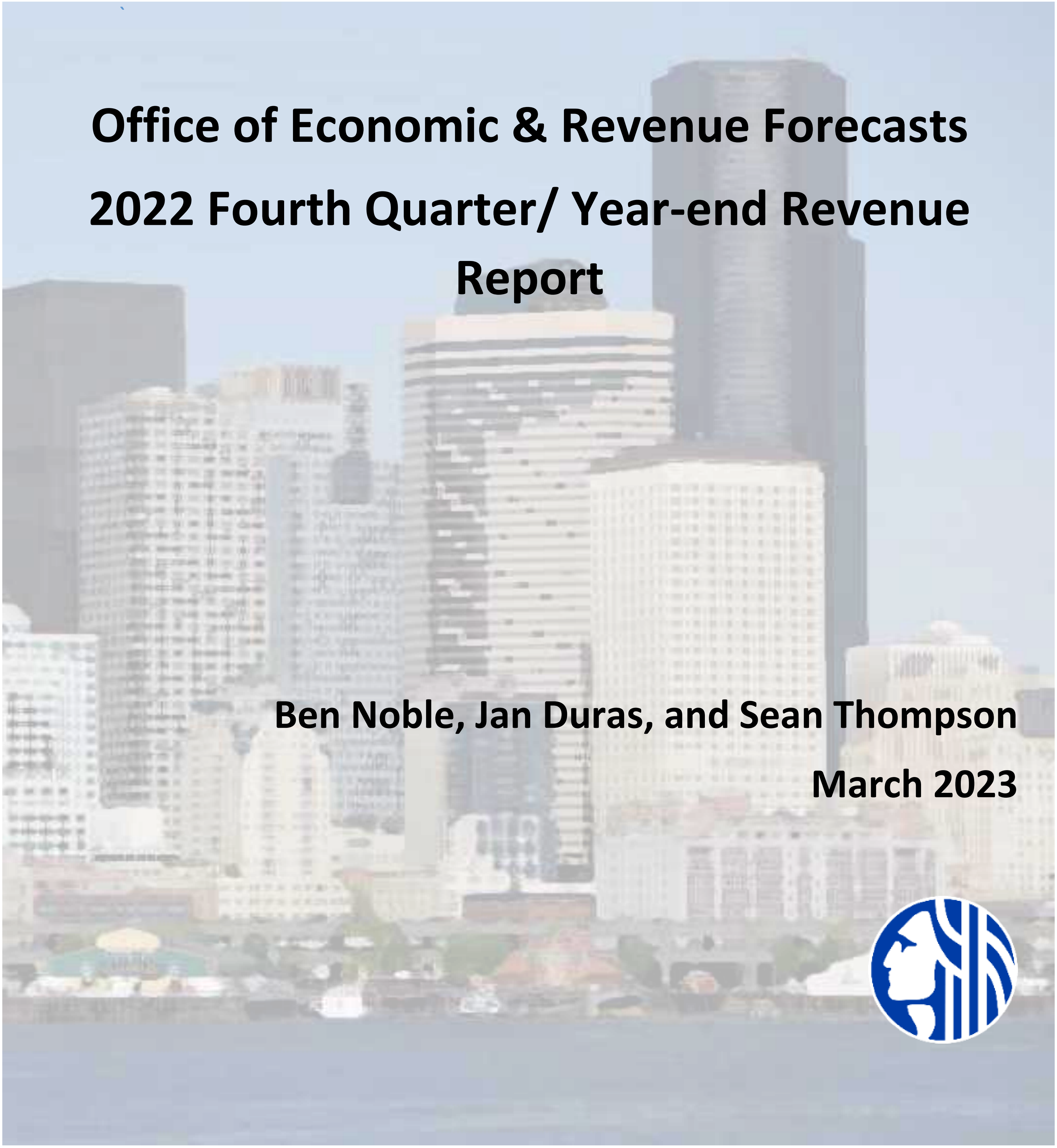


Office of Economic & Revenue Forecasts

2022 Fourth Quarter/ Year-end Revenue Report

Ben Noble, Jan Duras, and Sean Thompson

March 2023

1. Introduction

Structure and Schedule of Quarterly Revenue Reports. This represents the fourth and final quarterly revenue report that the Office of Economic and Revenue Forecasts (Forecast Office) will provide regarding 2022 revenues. This report documents revenues received through December 31st, 2022, as well as those received after this date but "accrued" to calendar year 2022 because they were payments for 2022 tax obligations.

The goal of the quarterly reports is to track actual revenue receipts relative to the levels anticipated by the most recent forecasts prepared by the Forecast Office. The results presented here are shown relative to the forecast approved by the City's Economic and Revenue Forecast Council on November 2nd of last year. This forecast update replaced the previous forecast, which had been approved on August 8th. In addition, because the fourth quarter result naturally serves as a year-end summary, this report also provides an opportunity to compare this year's results to those from the previous.

This additional component provides an opportunity to see how developments in the regional economy over the last twelve months have affected individual revenue streams and overall revenue trends. The report's structure and content differ somewhat from the previous three quarterly reports to accommodate this additional element. Following this introduction, Section 2 provides an overview of overall GF results, and analyses of the individual revenue sources that support this fund. It is important to recognize that these results only reflect the revenues earned by the GF. A full accounting of the GF's overall status also requires an assessment of the expenditure "side" of the ledger. The City Budget Office is responsible for tracking those expenditures and will separately be developing a year-end summary of overall GF status.

Section 3 shifts focus to selected non-GF Sources, including both the Jumpstart Payroll Expense Tax and Real Estate Excise Taxes. This section also provides analysis of other dedicated non-GF revenue sources, including the Sugar Sweetened Beverage Tax, the Short-Term Rental tax, and several transportation-specific funding sources.

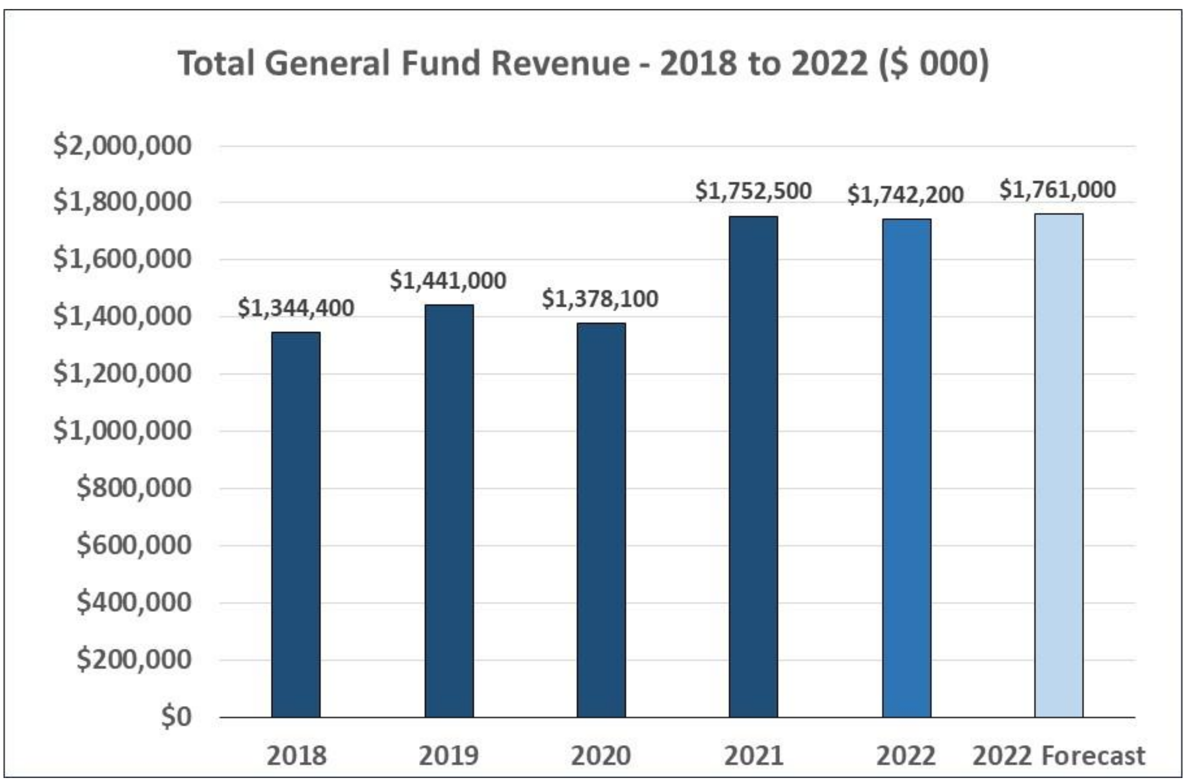
Timing of Report. In general, the Forecast Office aims to complete each quarterly report two weeks after the close of the quarter. However, the year-end, fourth quarter report is a notable exception from this pattern. This report cannot be completed until all the revenues attributable to 2022 have been reflected in the City's accounting system. Tax obligations for the preceding month and quarter are not generally due until 30 days after the close of the relevant month or quarter. In addition, the Washington State Department of Revenue does not distribute the City's share of December sales tax revenues until mid-February. As result, the City's financial books for the previous year are not closed until late

February so that all fourth quarter and annual tax payments can be "accrued" back to the previous year. This further implies that the fourth quarter revenue report cannot be completed until March of the following year, once the accrual process is complete.

2. Total General Fund Revenues and Highlights of Major Revenue Sources

2.1 Overall General Fund Revenues

As illustrated below, final General Fund (GF) revenues for 2022 fell somewhat short of forecast. In particular, the 2022 total of $1.742 billion is $19 million less than the November forecast of $1.761 billion. However, as detailed later in this section, this discrepancy was largely due to a timing issue related to the disbursement of certain grant revenues and reimbursement payments owed to the City. The City anticipates that these revenues will be paid in full over the course of 2023, once the associated services are delivered. So, this apparent revenue shortfall is just a shift in the timing of payments. Setting aside this issue, the remaining GF revenues actually exceed the November forecast by $22.6 million. While this is a significant amount of money, it represents less than 1.5% of total GF revenues, and thus demonstrates the overall accuracy of the forecast. (See the table on the page following for these specific results.) The chart below provides a visual comparison of the actual and forecast revenues for 2022, but also supplies additional context by depicting total GF Revenues for the period from 2018 to 2023.



- Note that prior to the pandemic the GF had shown strong annual growth of 7+% from 2018 to 2019.
- Overall revenues fell in 2020, even with the infusion of federal support, as the social distancing response to Covid-19 precluded a significant amount of taxable economic activity.
- While it appears that the GF made a remarkable recovery in 2021 it is important to recognize that the 2021 GF total includes nearly $250 million in revenue from the then newly authorized JumpStart Payroll Expense tax. GF revenues did generally prove to be resilient, but the GF total for 2021 included both the new JumpStart revenues and continued federal pandemic relief funding.
- For 2022, current JumpStart Payroll Expense Tax revenues were shifted out of the General Fund into their own separate fund. Nonetheless, the 2022 GF total does reflect some JumpStart Payroll Expense revenues. A total of almost $45 million in late payments of 2021 obligations were deposited in the GF during 2022. These deposits were consistent with policy direction provided by the City Council, which directed that all revenues related to 2021 obligations be deposited into the General Fund, no matter when they are actually received. In addition, the 2022 budget relied on the transfer of $85.4 million of 2022 Jumpstart Payroll Expense Tax revenues into the GF. While final 2022 GF revenues were still about $10 million less than the 2021 total, this decline would have been significantly larger without the late payments of 2021 payroll tax obligations and the additional transfer from the new JumpStart Fund.

Additional insights about how specific revenue sources contributed to overall GF performance relative to forecast and relative to 2021 are provided in the next subsections.

2.2 Individual General Fund Revenues – *Comparison to Forecast*

The table below provides additional detail about how specific GF revenue sources performed relative to November's forecast. As noted previously, with the clear exception of (i) Grants and (ii) Fund Balance Transfers, most GF revenues performed at or above their forecasted levels. A brief discussion of significant variations from forecast is provided in the text following the table.

2022 General Fund Revenues – Comparison to Forecast

Revenue Source	2022 Final Revenues	Forecast (Nov.)	Variance from Forecast	Percent of Forecast
Property Tax	$371,770	$371,630	$130	100.0%
Sales Tax	$331,220	$329,640	$1,590	100.5%
Business and Occupation Tax	$331,580	$326,620	$4,970	101.5%
Private Utility Taxes	$41,850	$42,920	($1,070)	97.5%
Public Utility Taxes	$192,850	$184,360	$8,490	104.6%
Other City Taxes	$14,540	$14,800	($260)	98.2%
Parking Meters	$23,860	$24,310	($450)	98.1%
Court Fines	$13,220	$12,810	$420	103.2%
Revenue from Other Public Entities	$23,080	$24,060	($980)	95.9%
Grants	$23,120	$59,800	($36,680)	38.7%
Fund Balance Transfers	$151,010	$155,910	($4,910)	96.9%
Service Charges and Reimbursements	$103,170	$99,460	$3,700	103.7%
Licenses, Permits, Interest, and (all) Other	$75,870	$71,350	$4,510	106.3%
Payroll Tax - Late 2021 Payments	$44,980	$43,400	$1,580	103.6%
Total General Fund Revenues	**$1,742,110**	**$1,761,060**	**($18,950)**	**98.9%**
Total - Less Grants and Transfers	**$1,567,990**	**$1,545,360**	**$22,630**	**101.5%**

- **Property, Sales, and B&O Tax.** Note for all three of the largest revenue sources, final 2022 receipts equaled or exceeded forecasts:
  - Property tax totals were essentially equal to the forecast, with a difference of less than $150,000 “to the good”.
  - Retail Sales Tax revenues exceeded forecasts by just over $1.5M, reflecting a forecast error of less than 0.5%.
  - Business and Occupation Tax revenues exceeded the forecast by $5M, or 1.5%.
- **Public Utility Taxes.** Actual revenues exceeded the forecast by almost $8.5M. The largest share of this overperformance is due to an unexpected increase in City Light utility tax revenue due to higher heating load from a cold snap in November and December.
- **Grants.** Much of the variance in grant revenues is driven by appropriation automatically carried forward from the previous year and the assumption that it will be used within the current year. In reality, grants are commonly spent down over multiple years and revenues flow in accordingly. Over the coming year, CBO will be working with departments to refine the process of tracking grant revenues and to improve the accuracy of these forecasts.
- **Fund Balance Transfers.** The November forecast assumed that 2022 fund balance transfers would total $156M, including $85+M of revenue from the JumpStart

Payroll Tax and $66M of CLFR funding. The latter amount fell short by $5M due to delays in the implementation of some projects that qualify for revenue replacement. However, this should only be a matter of timing, and the City anticipates capturing the remaining revenues in 2023.

- **Service Charges and Reimbursements.** This revenue category reflects payments for services or the City being reimbursed for direct costs. The additional $3.7M reported in this category was generated by the Seattle Fire Department for unanticipated COVID-related activities and parking enforcement at special events.
- **Licenses, Permits, Interest Income and Other**. The $4.5M in additional revenue in this category is largely due to increased interest earnings associated with increasing rates. In addition, there was some miscommunication between SPD and CBO regarding anticipated payments for some services provided by SPD that resulted in higher than projected revenues in this category.

2.3 Individual General Fund Revenues – *Comparison to 2021*

Shifting to a comparison to 2021, the table below reports final 2022 revenues relative to the year previous, and the rate of annual growth associated with each.

2022 General Fund Revenues – Comparison to 2021

Revenue Source	2021 Year-End Actual Revenues	2022 Year-End Actual Revenues	Year/Year Difference ($)	Year/Year Difference (%)
Property Tax	$363,690	$371,770	$8,080	2.2%
Sales Tax	$299,410	$331,220	$31,810	10.6%
Business and Occupation Tax	$315,390	$331,580	$16,190	5.1%
Private Utility Taxes	$44,720	$41,850	($2,870)	(6.4%)
Public Utility Taxes	$175,140	$192,850	$17,710	10.1%
Other City Taxes	$20,820	$14,540	($6,280)	(30.2%)
Parking Meters	$16,510	$23,860	$7,350	44.5%
Court Fines	$18,610	$13,220	($5,390)	(29.0%)
Revenue from Other Public Entities	$21,600	$23,080	$1,480	6.9%
Grants	$69,420	$23,120	($46,300)	(66.7%)
Fund Balance Transfers	$44,680	$151,010	$106,330	238.0%
Service Charges and Reimbursements	$42,840	$103,170	$60,330	140.8%
Licenses, Permits, Interest, and (all) Other	$71,410	$75,870	$4,460	6.2%
Payroll Tax (2022 GF are Late 2021 Payments)	$248,220	$44,980	($203,240)	N/A
Total General Fund Revenues	**$1,752,450**	**$1,742,110**	**($10,340)**	(0.6%)
Total w/o Grants, Fund Balance Transfers Service Charges, and Payroll Tax	**$1,347,300**	**$1,419,840**	**$72,540**	5.1%

Overall, these results highlight how the local economy has continued its recovery from the Covid-19 pandemic.

- **Property Tax.** Property tax revenues are constrained by state law to grow at a maximum rate of 1%, plus the new value of new construction. In this context, annual growth of 2.2% is actually quite strong, indicating that new construction increased the total assessed value of property in the City by 1.2%.
- **Sales Tax.** Although sales tax showed annual growth of 10.6%, it is important to recognize that regional inflation increased overall prices by 9%, so real growth constituted a modest 1.6%.
- **B&O Tax.** Annual growth was a solid 5.1%, but as noted immediately above this actually represents a decline in real terms, after correcting for the 9% local inflation rate. However, B&O payments have also been affected by changes in the timing of required payments for quarterly and annual filers. This has resulted in the delay of some 2022 payments.
- **Utility Taxes.** Private utility taxes declined relative to 2021 as demand for both telephone and cable services continues to decline. Strong demand for City Light and SPU services, driven by warm weather in the summer and cold in the winter, contributed to significant growth in public utility tax revenues.
- **Other City Taxes.** While it appears that there was a significant decline in this category, this is simply the result of a shift in the accounting of admissions tax revenues. In 2021 these revenues were included in the GF, while in 2022 they were shifted into the Arts and Culture fund.
- **Parking Meters.** As the social distancing associated with Covid-19 eased, demand for parking increased and, per City policy, SDOT began to raise parking meter rates in response. The net effect was a $7+million increase in parking tax revenues.
- **Court Fines.** The decline in court fines is most directly associated with the refund of several million dollars in parking fines that resulted from the City's Parking Enforcement Officers not operating with the necessary legal authority for a period of several months. This City has addressed this issue and no more refunds are expected.

The remaining differences are associated with several one-time revenue opportunities and policy changes. For example, payroll tax revenues associated with 2021 obligations were deposited in the General Fund, while obligations for 2022 and beyond will be directed into a new stand-alone fund. In addition, 2021 GF revenues included a one-time payment of

$60 million associated with the sale of the Mercer meg-block. If one sets those policy changes and one-time revenues aside, a comparison of the remaining categories shows that these core GF revenues grew by 5.1% relative to 2021. While strong in absolute terms, this does represent a modest decline in inflation-adjusted terms, and highlights one aspect of the challenges faced in developing a sustainable budget to support existing City operations.

3. Select Non-General Fund Revenue Sources

In addition to its work in forecasting and tracking the full range of GF revenues, the Forecast Office also closely tracks a select group of non-GF sources. The tables presented in Sections 3.3 and 3.4 provide summary-level information for most these non-GF revenues, including several that support general government functions (Section 3.3) and some that are specifically dedicated to transportation purposes (Section 3.4). In advance of this summary presentation, Sections 3.1 and 3.2 present detailed discussion and analysis of the two largest non-GF sources that fall within the Forecast Office's purview; namely the JumpStart Payroll Expense Tax and the Real Estate Excise Tax.

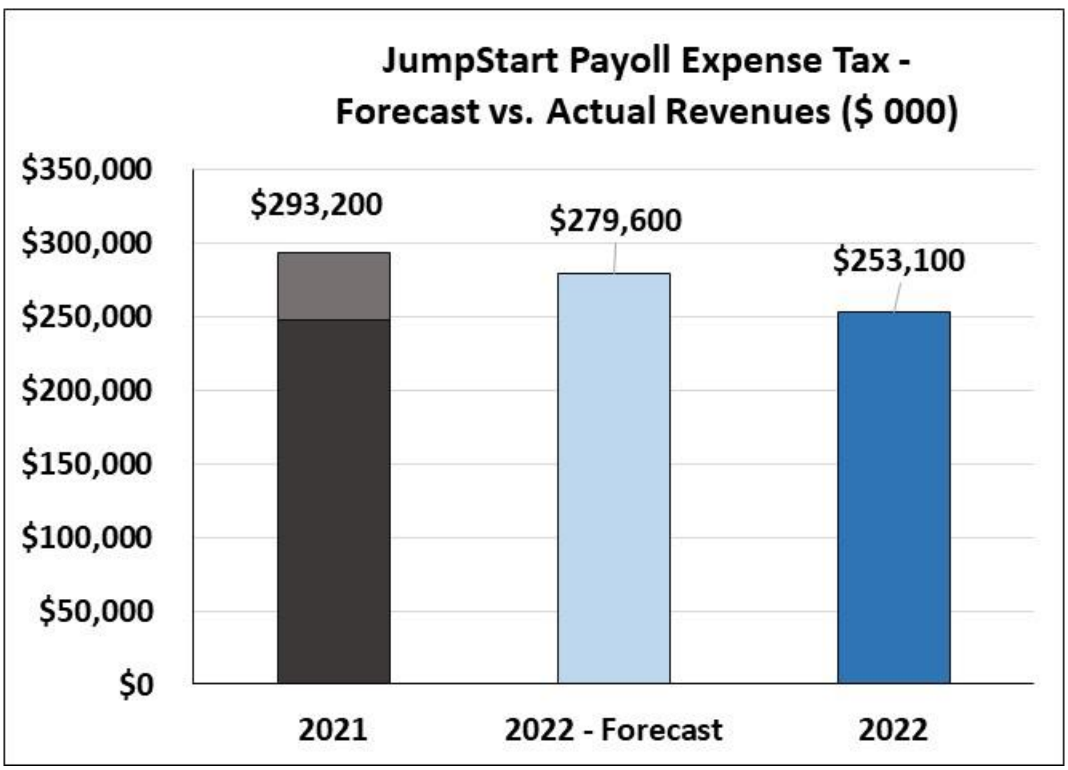
3.1 JumpStart Payroll Expense Tax

First applied in 2021, the Payroll Expense Tax imposes a tax of between 0.7% and 2.4% on the wages paid to higher compensated employees working at relatively large companies. The tax rate increases with individual compensation and with the overall payroll of the company. For 2021, payments were not due until the first part of 2022. This shifted to quarterly payments for 2022.

Final 2021 revenues ultimately totaled $293 million. When the City's accountants "closed" the books for 2021, payments totaled $248 million, but an additional $45 million in late payments for 2021 tax obligations was received over the remainder of 2022. In terms of revenue earned, these results put this tax almost on par with property, sales, and B&O taxes. However, the payroll expense differs significantly from these other major revenue sources in that it is paid by relatively few firms. For example, in 2022, 70% of the revenues were generated from just ten companies, with eight of these ten companies operating in the same sector. This concentration creates significant inherent volatility in this revenue stream. Changes in the financial fortunes of individual companies can materially impact overall revenues.

The initial 2021 results served as a key input to into the updated forecasts of 2022 revenues that were developed in April and August of last year. Although initially the Forecast Office raised the forecast, as the technology sector began to cool, stock values fell, and employment growth slowed, the 2022 forecast was revised and reduced for the August update. In developing the November Forecast update, the Forecast Office concluded that there was insufficient information to support a specific forecast revision, but did advise that a variety of signals indicated that the 2022 revenues were likely to fall short of forecast. Public announcements had been made by several firms regarding layoffs or hiring freezes, and the stock values of many of the largest payers had continued to decline. The latter is important because for many employees the total compensation subject to the tax includes the value of annual stock grants, and that share of compensation was in decline.

The table below provides a comparison of final 2021 and 2022 revenues, as well as a comparison of 2022 actuals to the final 2022 forecast.



- For 2022, JumpStart Payroll Tax revenues totaled $253M. As illustrated above, this is *$40M* less than the $293M ultimately received for 2021, and *$26.5M* less than the $279M that was forecast for 2022. Recall that this was the August forecast, which was not updated in November.

- As highlighted by the lighter portion of the two-tone column for 2021, a significant share of 2021 revenues were received after February 2022, as a number of firms took some time to understand and calculate their liabilities under the new tax. We do not anticipate the same pattern for 2022 revenues as there do not appear to be significant payments outstanding at this point. Almost all firms that paid in 2021 have made 2022 payments, and almost all the firms that made third quarter 2022 payments have also made fourth quarter payments.
- As noted above, the decline in revenues relative to 2021, and relative to forecast, generally reflects the changes in employment and compensation patterns in the technology sector, which is responsible for a large share of overall payroll expense tax revenues. During 2022, technology sector employment was stagnant or falling, and with stock prices in sharp decline, individuals' compensation also fell.
- The persistence of work-from-home arrangements may also explain some of the year-over-year decline. As these work arrangements become more long-term, firms have developed an increased incentive to track exactly where employees are working. Payroll taxes do not apply to work that is conducted outside the City, or to employees who are "primarily assigned" to a non-City location where they spend at least 51% of their work hours.

The Forecast Office is currently working on a number of fronts, including with the Washington State Department of Employment Security, to develop better forecasts of future payroll expense tax revenue.

3.2 Real Estate Excise Tax (REET)

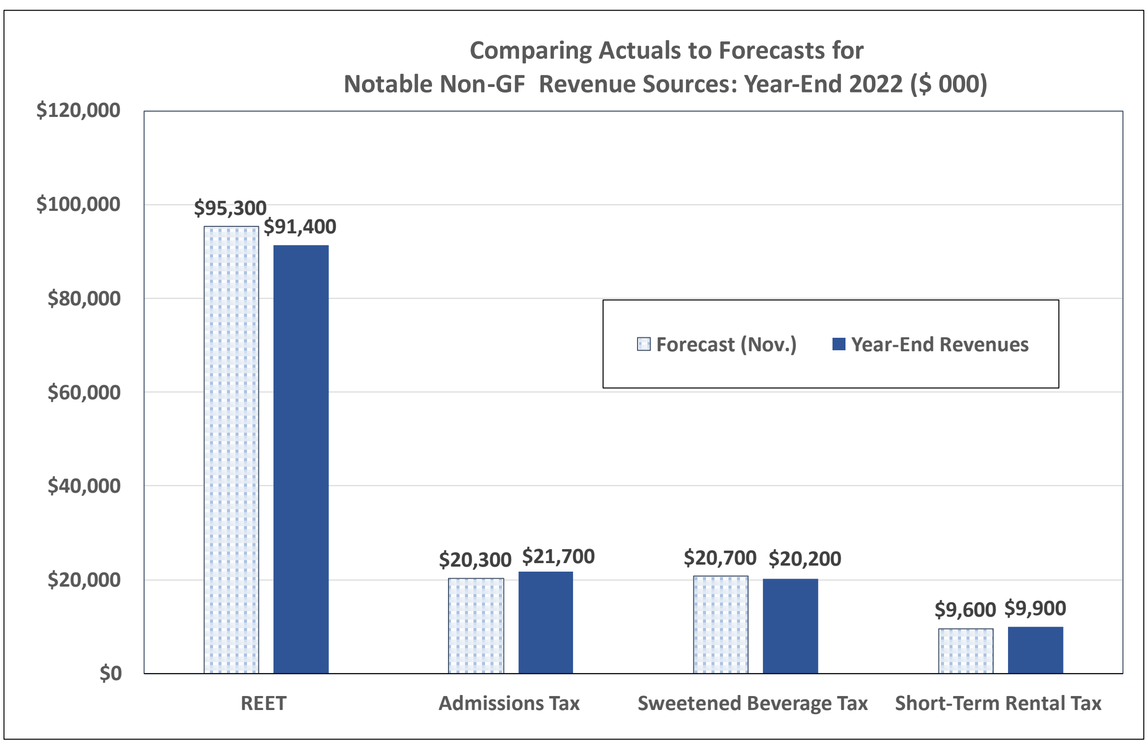
REET applies to every property transaction that occurs within the City of Seattle. The tax is composed of two separate 0.25% taxes (for a total of 0.5%), which can each be used for different capital purposes. Final results for 2021 showed that REET generated a record $112M in 2021. Informed by that result, the April forecast for 2022 REET revenues was increased to $99.7 million, and increased again to $106.6 million with the August forecast. The latter update was based on data regarding actual data through June of 2021, which showed a very robust real estate sector; increasing prices and high transaction volumes were contributing to strong revenue results.

However, in the third quarter, market conditions changed quickly. A sharp upward turn in interest rates made mortgage financing significantly more costly, and at the same time talk of hiring freezes and layoffs in the technology sector created some degree of financial uncertainty for an important subset of potential residential real estate buyers. On the commercial side, uncertainty about the long-term impact of work-from-home combined with the same increase in financing costs to discourage transactions. This led to a revision in the November forecast, with the 2022 prediction reduced to $95.2 million.

Ultimately, 2022 revenues fell short of even that revised forecast, reaching a final total of $91.4 million. Unfortunately, the trend seen late in 2022 has extended into the early part of this year, with less than $6 million generated in January and February, combined. These results will inform the upcoming April forecast update, and likely lead to a downgrade in the REET forecast for 2023, and possibly 2024 as well.

3.3 General Government Non-GF Revenues

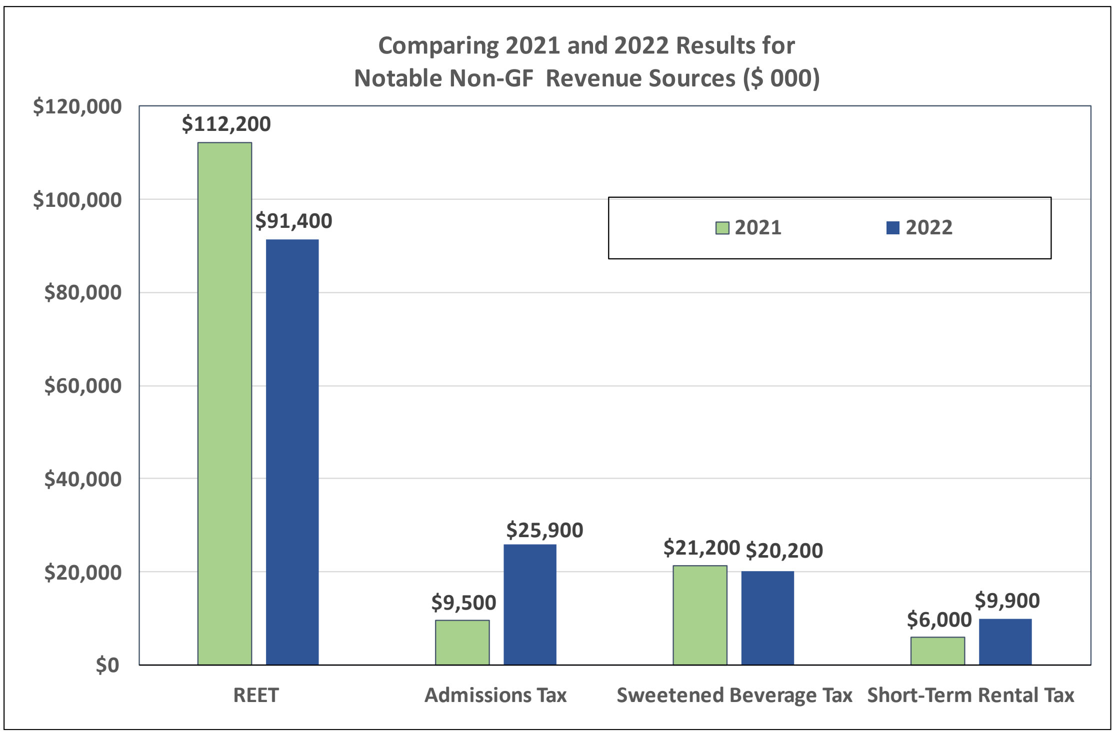
The Forecast Office tracks multiple non-GF revenue sources. The results presented in this subsection focus on three that support "general government" activities. These include the Admissions Tax, the Sweetened Beverage Tax (AKA the "soda tax"), and the Short-term Rental Tax. City policy, as established by ordinance, directs each of these sources to a set of dedicated general government purposes. The chart below compares the 2022 year-end results for each to the final November forecasts. REET revenues are included in these charts because traditionally the Forecast Office has included them among this group of general government non-GF sources. Given the magnitude of REET revenues and the significant developments affecting those revenues, a thorough explanation of the REET results shown below here are provided in the preceding, dedicated section.



In general, these revenue sources tracked very closely to our November forecasts.

- Admissions tax revenue slightly outpaced our last forecast, producing an additional $1.4M in revenue.
- Revenues from the Sweetened Beverage tax fell about $500K short of forecast.
- Short-Term Rental Tax revenues exceeded forecasts, but by just $300K.

And when compared to 2021, these revenue sources generally reflected the ongoing recovery from Covid-19 related restrictions. Given the impacts on large entertainment events (Admissions Tax), restaurant activity (Sweetened Beverage Tax), and tourist travel (Short-term Rental Tax), each of these sources had been significantly negatively impacted by the pandemic.



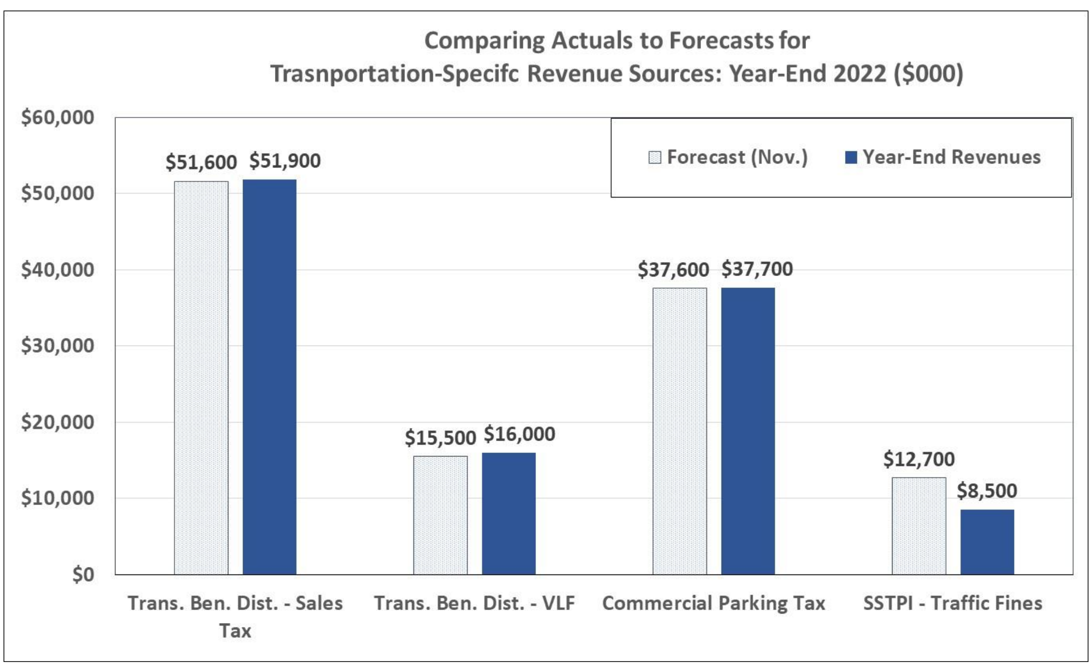
- The rather dramatic increase in Admissions Tax revenue can partially be explained by the easing of Covid-19 restrictions during 2022, but the biggest impact was from the full-year operation of the newly opened/re-opened Climate Pledge Arena. The facility was operational in 2021, but only for two months.
- Sweetened Beverage Tax revenues fell by $1 million relative to 2021. However, this is not a reflection of actual consumption across the years, which has been increasing. Due to annual accounting adjustments (accruals) between 2020, 2021, 2022 and the beginning of 2023, the timing of receipts led, on net, to larger recognition of revenues in 2021 than 2022. Consumption data indicates that

consumption in calendar year 2022 exceeded consumption in 2021. This is mirrored in the data on restaurant activity, which is one major source of sweetened beverage sales, and which increased in 2022, relative to 2021.

- The significant increase in Short-term Rental Tax revenue reflects the strong recovery of the hospitality sector, and in particular the market of "Airbnb-style" services.

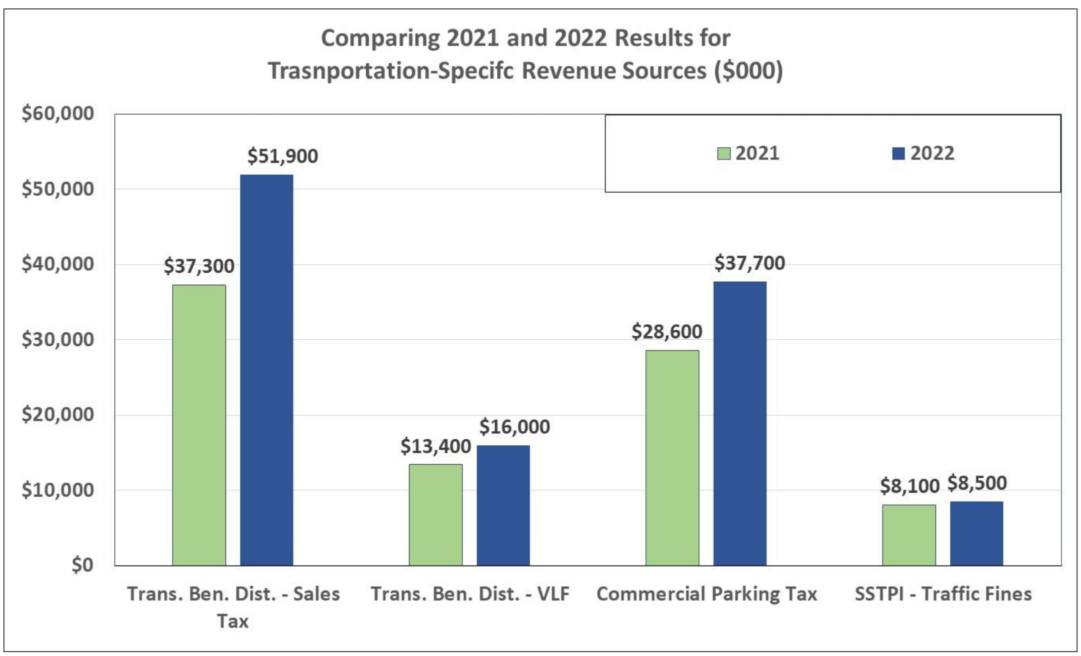
3.4 Transportation-Specific Non-GF Revenues – Comparison to 2022 Forecast and 2021 Results

Funding for the Seattle Department of Transportation (SDOT) comes from a variety of sources, including a few dedicated revenue streams. Two of the most significant sources – a 0.15% Sales Tax and a $40 Vehicle License Fee (VLF) – originated under the authority of the Seattle Transportation Benefit District (STBD). While the STBD originally existed as a stand-alone taxing authority, following changes in state law it has now been fully integrated into City operations. In addition, the City's Commercial Parking Tax revenues are dedicated to transportation purposes, as are all the revenues generated from school zone cameras and a share of the fines collected from automatic red-light enforcement cameras. As shown in the following two charts, these revenue sources generally outperformed forecast, if only marginally, and all exceeded their 2021 levels, several by significant amounts.



- As noted above, Seattle's Transportation Benefit District (STBD) relies on two primary revenue sources: a 0.15% increment of Retail Sales Tax and an annual Vehicle License Fee (VLF).
- Per the chart to the above, both have generated revenues slightly above forecast, with the Sales Tax overperforming by $300K and the VLF by about $500K
- Commercial Parking Tax revenues, which are also dedicated to transportation purposes, tracked very closely to the November forecast, producing $100K more than expected.
- Unfortunately, these net gains were more than offset by a $4M+ shortfall in school-zone and red-light camera revenue, relative to forecast. Staffing shortages at the Seattle Police Department (SPD) led to this outcome. All incidents must be reviewed in a timely manner before a ticket can be issued, and SPD struggled to make this a priority. However, staff have now been assigned and such tickets are being processed promptly.

Compared to last year, the final revenues from each of these sources also demonstrate how the local economy continues its strong recovery.



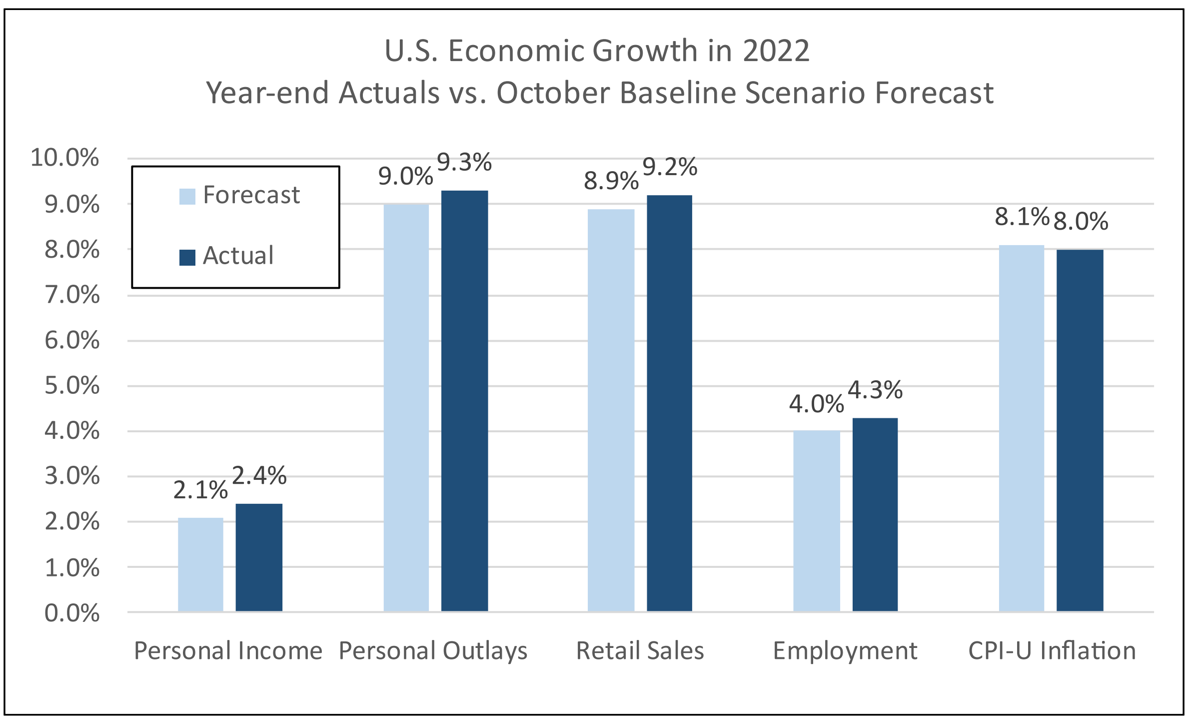
- Although the growth in STBD sales tax revenues appears remarkable, much of the year-over-year growth is due to an increase in the tax rate from 0.1% to 0.15%. This change occurred mid-year and drove much of the revenue growth. That said even if the rate had been constant, revenues would have grown relative to 2021, consistent with the overall growth in City sales tax revenues.

- A change in tax rates also drove some of the growth in Commercial Parking Tax Revenues. In July of 2022, the tax rate increased from 12.5% to 14.5%. Nonetheless, the 30+% revenue increase, relative to 2021, was mainly due to increased parking activity.
- Revenues from school-zone and red light cameras only grew modestly from 2021, but as noted above staffing issues at SPD had a significant impact in reducing 2022 revenues.

4. Overview of Economic Climate

To provide some additional context for the revenue results presented in this report, this final section provides an overview of recent economic developments, with a specific focus on how conditions have evolved since October and November, when the most recent forecast was developed. In general terms, the economic news since last fall has been consistent with the trends, we saw emerging early in the third quarter of 2021.

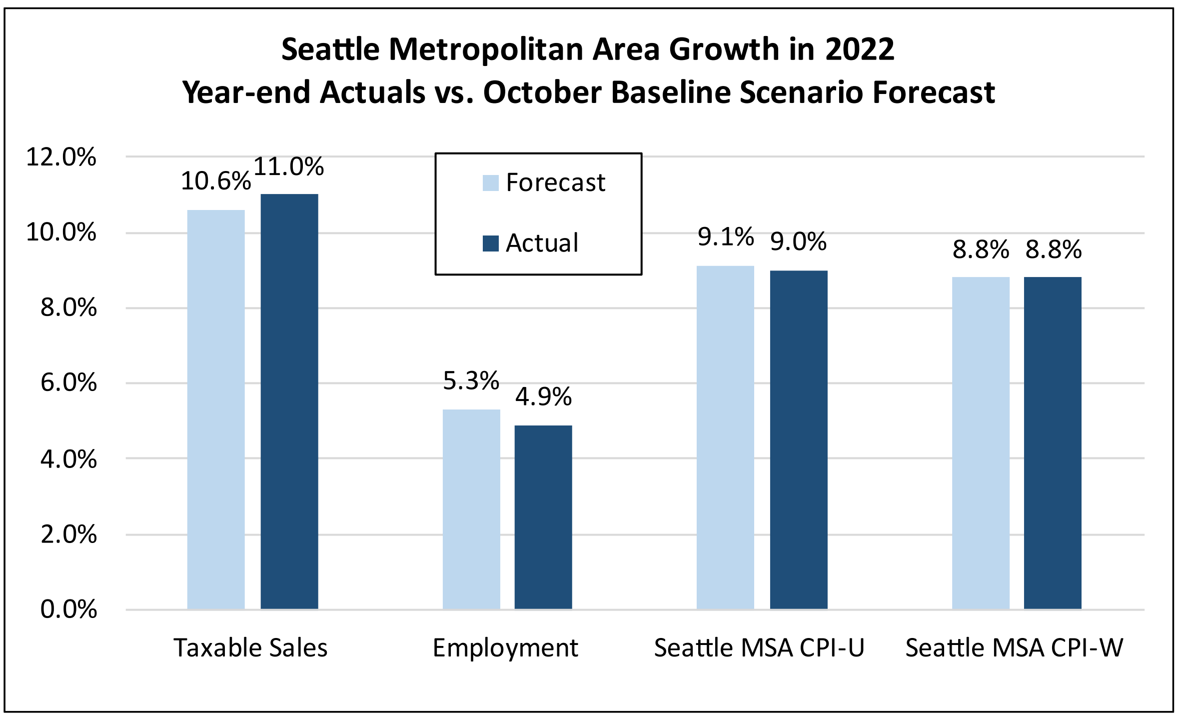
Focusing first on the national economy, the chart below compares the final forecasted values of some of the key economic metrics that serve as inputs to the Forecast Office's regional economic model. These forecasts were provided by IHS Markit and represent their expectations as of October last year.



- As noted immediately above, the national-level financial metrics presented here are ones that the Forecast Office incorporates into our regional economic modeling. Thus, their performance relative to forecast can help explain the divergence between predicted and actual revenues.

- Consistent with the small deviations in our revenue forecasts, personal income, outlays, and retails sales have outperformed expectations from the November economic forecast, but not by dramatic amounts.
- Despite increased uncertainty and the apparent risk of a recession, the labor market has been more resilient than expected. The strong labor market is one reason that many recession forecasts have been moderated and/or delayed.
- Inflation is still high, but IHS Markit anticipates inflation to moderate over 2023 as supply-chain issues are addressed and the impact of falling rents is reflected in the various prices indexes that measure inflation.

A comparable comparison looking at our forecasts of key regional metrics reveals similar results. Final year-end results show that the regional economy showed the growth we anticipated and actually outperformed our expectations in terms of taxable sales. That said, hiring slowdowns and layoffs emerged in the local technology sector late in the year, and this development is likely to slow regional growth over the next few years.



- The regional economy has shown the same strength as we have seen at the national level. For example, in line with the developments in the national economy, regional sales grew in 2022 somewhat faster than we forecast in the fall, and this helps explain the strength of both retail sales and B&O revenues.

- Regional employment grew somewhat less than forecast, potentially reflecting the slowdown in what had been the technology sector's fast hiring pace of the last few years.
- Regional inflation continues to outpace the national rate, but current trends suggest that it has also begun to decline.