Office of Economic & Revenue Forecasts

2023 Q4 / Year-end Revenue Report

March 2024

1. Introduction

Structure of Quarterly Revenue Reports. This represents the final quarterly revenue report that the Office of Economic and Revenue Forecasts (Forecast Office) provides regarding 2023 revenues. This report documents revenues received in general through December 31, but also some revenues which were received after this date, by the end of February, and were accrued to fiscal year 2023, because they were payments for 2023 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 October 17th of last year. This forecast update replaced the previous forecast, which had been approved on August 10th. In addition, because the fourth quarter results serve as a year-end summary, this report also provides an opportunity to compare this year's results to those from the previous year.

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 General Fund (GF) results, and analyses of the individual revenue sources that support this fund. It is important to recognize that these results only reflect the revenue side of the GF. A full accounting of the GF's overall status however 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-General Fund revenue streams, primarily Jumpstart Payroll Expense Tax, Real Estate Excise Tax, but also other dedicated revenue sources, including the Sugar Sweetened Beverage Tax, the Short-Term Rental tax, and several transportation-specific funding sources.

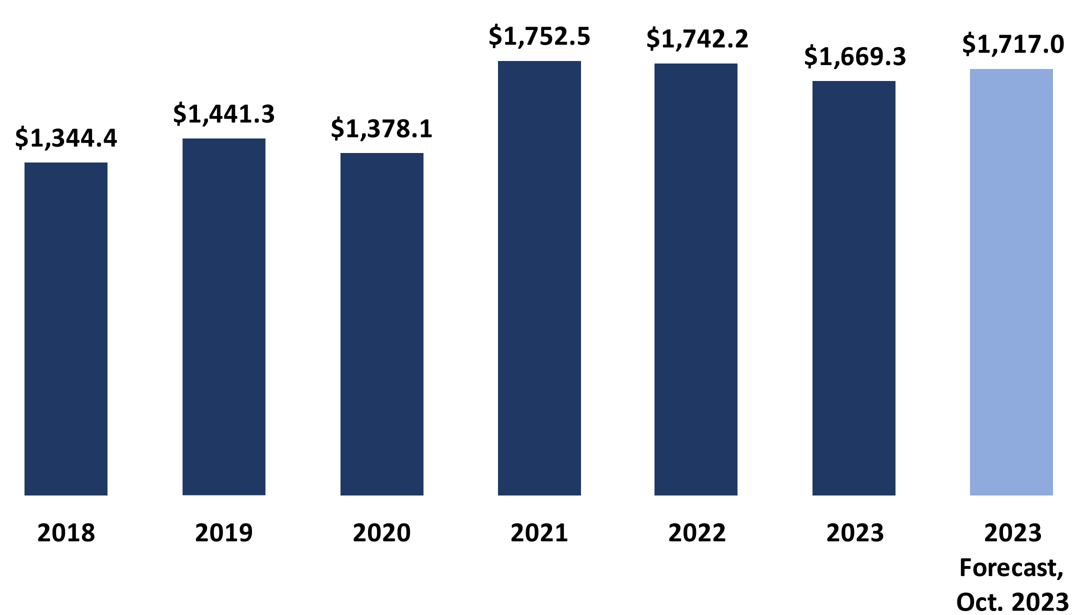
Timing of Report. In general, the Forecast Office aims to complete each quarterly report two weeks after the close of the quarter. However, the year-end, fourth quarter report is a notable exception to this pattern. This report cannot be completed until all the revenues attributable to 2023 have been 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 distributes only in mid-February the City's share of sales tax revenues for December obligations that taxpayers have to remit by the end of January. As a result, the City's financial books for the previous year are not closed until early March so that 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 shown and discussed below, final General Fund (GF) revenues for 2023 fell somewhat short of the forecast. In particular, the 2023 total of $1.669 billion is $48 million less than the October forecast of $1.717 billion. However, as detailed later in this section, this discrepancy is largely due to a timing issue related to the disbursement of certain grant revenues. The City anticipates that these revenues will be paid in full, 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 underperformed the October forecast by $8 million. While this is a significant amount of money, it represents just a half percent of total GF revenues. In addition, as discussed in more detail further below, due to some accounting issues about $8 million of 2023 obligations for public utility taxes will only be included in GF revenues in 2024. Complicating the comparisons further, a $3.9 million in payroll expense tax refunds that the October forecast anticipated to lower 2023 GF revenues was only processed in January and will affect 2024 GF revenues instead.

Total General Fund Revenue ($ millions)



- Note that prior to the pandemic the GF had shown strong annual growth of 7.2% 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.
- Starting with 2022 obligations, Payroll Expense Tax revenues were shifted out of the General Fund into their own separate fund. Nonetheless, the 2022 GF total does reflect some Payroll Expense Tax revenues, as $44.5 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 received. In addition, the 2022 budget relied on the transfer of $85.4 million of 2022 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 Payroll Expense Tax Fund.
- The 2023 GF total again includes some Payroll Expense Tax revenues, but to a smaller degree than in 2022. Late payments for 2021 obligations decreased from $44.5 million to just $3.6 million, and the transfer of payroll expense tax revenues from Payroll Expense Tax Fund to the general fund went from $85.4 million to $69.8 million. Thus, about $56.5 million of the $72.9 million decline in the GF revenues shown in the chart above is due to these two effects.

Additional insights about how specific revenue sources contributed to overall GF performance in 2023, both relative to forecast and relative to 2022, are provided in the next subsections.

<u>2.2 Individual General Fund Revenues – Comparison to Forecast</u>

The table below provides additional detail about how specific GF revenue sources performed relative to October's forecast. A brief discussion of variations from forecast is provided in the text following the table.

Table 1. 2023 General Fund Revenues – Comparison to Forecast

Revenue Source	2023			
	Forecast Oct. 2023, $ mil.	Actual Revenues, $ mil.	Variance from Forecast, $mil.	Variance from Forecast, %
Property Tax (Including Medic One Levy)	$379.3	$377.8	-$1.5	-0.4%
Retail Sales Tax	$348.0	$339.9	-$8.1	-2.3%
Business & Occupation Tax	$355.4	$356.2	$0.8	0.2%
Utility Tax - Private	$42.6	$43.2	$0.7	1.6%
Utility Tax - Public	$192.9	$185.7	-$7.2	-3.7%
Other City Taxes	$13.8	$14.1	$0.3	2.0%
Parking Meters	$36.6	$37.0	$0.3	0.9%
Court Fines	$22.3	$24.0	$1.7	7.5%
Revenue from Other Public Entities	$18.9	$19.1	$0.2	0.9%
Grants	$73.3	$34.1	-$39.2	-53.4%
Fund Balance Transfers	$81.3	$80.5	-$0.8	-1.0%
Service Charges & Reimbursements	$76.0	$76.2	$0.2	0.2%
Licenses, Permits, Interest Income and Other	$77.0	$77.6	$0.6	0.8%
Payroll Tax	-$0.4	$3.6	$4.1	
Total General Fund	**$1,717.0**	**$1,669.1**	**-$48.0**	**-2.8%**
Total General Fund Less Grants and Transfers	**$1,562.4**	**$1,554.4**	**-$8.0**	**-0.5%**

- **Property Tax** totals were somewhat below the forecast, with a difference of less than 0.4% or $1.5 million.
- **Sales Tax** revenues underperformed the forecast notably and ended nearly $8.1 million or 2.3% below the anticipated level. The October forecast expected a decline in sales tax revenue from construction in 2024, but it materialized already in the second half of 2023. Taxable sales in other sectors showed surprising weakness in the second half of 2023 as well, and in several cases actually declined year-over-year in the last couple of months.
- **B&O Tax** Business and Occupation Tax revenues exceeded the forecast slightly, by $0.8 million, or 0.2%.
- **Public Utility Taxes.** Actual revenues came in under the forecast by almost $7.2 million. About $2.3 million of this gap is the result of an accounting error that removed the March water tax revenue transfer from the system. An additional $5.7 million of the shortfall is due to an accounting oversight in which December electric tax payments – due in January – were not accrued back to 2023. Had it not been for these two accounting errors, totaling about $8 million, overall public utility revenues would have end up $0.8 million above the forecast. The $8 million of “missing” revenues will be included in 2024 GF.
- **Grants.** Much of the variance in grant revenues is driven by the way grants are appropriated, spent and reimbursed. Generally, departments receive appropriations and assumed revenues for the full amount of the grant in the year

the grant is awarded, and those appropriations are built into the budget and their financial plans. As most grants are spent down over multiple years, with revenues flowing in accordingly, only a portion of the total reimbursement is received and a large amount of appropriation authority is carried forward from year to year. All of the under-collection in grants in 2023 is this unspent and, as yet unreimbursed appropriation and will be reflected in following forecasts.

- **Fund Balance Transfers.** The October forecast assumed that 2023 fund balance transfers would total $81.3 million, consisting primarily of the $69.8 million of revenue from the JumpStart Payroll Expense Tax Fund and $8.9 million of Coronavirus Local Fiscal Recovery (CLFR) funding. The actual 2023 amount is just $0.8 million lower.
- **Licenses, Permits, Interest Income and Other**. A lot of payments for business license renewals made in 2022 were only receipted in 2023 due to system issues. The extent to which this was the case appears to have been underestimated, as a result business license fees generated about $2.8 million of revenue above the forecast. This was however partially offset by lower than anticipated revenues from other sources in this category.
- **Payroll Expense Tax** Starting with 2022 obligations, JumpStart Payroll Expense Tax receipts were shifted out of the General Fund into their own separate fund, but all revenues related to 2021 obligations continue to be deposited into the General Fund. In 2023, there were still some late payments made for 2021 obligations and the some refund requests for these obligations were received as well. The October forecast anticipated a $3.9 million refund to be finalized by the year-end, as reflected by the -$0.4 million shown for Payroll Expense Tax in GF revenues Table 1 above. Because the refund payment was completely accounted for only in January 2024, the 2023 actual GF revenue exceeded the forecast by $4.1 million and the refund will lower 2024 GF revenue instead.

2.3 Individual General Fund Revenues – Comparison to 2022

Shifting to a comparison to 2022, the table below reports final 2023 revenues relative to the year previous, and the rate of annual growth associated with each.

Table 2. 2023 General Fund Revenues – Comparison to 2022

Revenue Source	2022 Actual Revenue, $mil	2023 Actual Revenue, $mil	Year/Year Change, $mil	Year/Year %
Property Tax (Including Medic One Levy)	$371.8	$377.8	$6.0	1.6%
Retail Sales Tax	$331.2	$339.9	$8.7	2.6%
Business & Occupation Tax	$331.6	$356.2	$24.5	7.4%
Utility Tax - Private	$41.9	$43.2	$1.4	3.3%
Utility Tax - Public	$192.8	$185.7	($7.2)	(3.7%)
Other City Taxes	$14.5	$14.1	($0.4)	(2.9%)
Parking Meters	$23.9	$37.0	$13.1	55.0%
Court Fines	$13.3	$24.0	$10.7	79.9%
Revenue from Other Public Entities	$18.4	$19.1	$0.6	3.5%
Grants	$23.3	$34.1	$10.8	46.4%
Fund Balance Transfers	$150.9	$80.5	($70.4)	(46.7%)
Service Charges & Reimbursements	$132.5	$76.2	($56.3)	(42.5%)
Licenses, Permits, Interest Income and Other	$50.9	$77.6	$26.7	52.5%
Payroll Tax	$45.0	$3.6	($41.3)	(91.9%)
Total General Fund	**$1,742.1**	**$1,669.1**	**($73.0)**	**(4.2%)**
Total General Fund Less Grants and Transfers	**$1,567.8**	**$1,554.4**	**($13.4)**	**(0.9%)**

- **Property Tax.** Medic 1/EMS levy revenues declined $4.3 million, this was however more than offset by the growth in the general expense levy which increased by $10.3 million, resulting in a $6 million increase in General Fund property taxes relative to 2022 collections. Property tax revenues are constrained by state law to grow at a maximum rate of 1%, plus the new value of new construction, which accounts for the growth in the general expense levy. The amount of Medic 1/EMS levy received by the City is dependent on the relative growth in King County and City of Seattle assessed values.
- **Sales Tax** revenues grew a rather modest 2.6%, below the 5.7% inflation rate. Taxable sales in construction sector grew only 1.3% and those in trade declined about 0.3% year-over-year. Leisure and hospitality became the strongest growing sector, with a 10.4% increase from 2022.
- **B&O Tax.** With a tax base more diversified than sales tax, the annual growth of business and occupation tax revenues was a solid 7.4%, this represents a 1.7% increase in real terms, after correcting for the 5.7% local inflation rate.

- **Utility Taxes.** Private utility taxes increased relative to 2022, resulting in a 3.3% growth year over year. Several accounting issues with the accrual of 2023 revenues and with a $4.9 million refund to Seattle City Light distort the true year-over-year change in public utility revenues, by increasing the 2022 revenues and decreasing 2023 revenues. Adjusting for these issues, the public utility tax revenues grew about $10.6 million, or 5.7%, between 2022 and 2023.
- **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. Due to gradual return to the office, parking meter revenues continue to beat expectations for 2023.
- **Court Fines.** Court fine revenues were artificially low in 2022 due most directly to 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. Referral of unpaid citations to collections had also not yet been reinstated post COVID-19 suspension of collections. In 2023, the City addressed the authority issue and the reintroduction of collections was preceded by an amnesty period, which yielded a one-time increase in revenues. Overall, parking-related citation revenues increased approximately $11.1 million over 2022. Red Light Camera enforcement revenues also increased in 2023 by $1.9million. These increases were offset by a $2.4 million decrease in penalty fees.
- **Fund Balance Transfers** declined $70.4 million year-over-year as a result of a $15.6 million smaller transfer of payroll expense tax revenues from the JumpStart Payroll Expense Tax Fund to the General Fund and $57.4 million less in CLFR funding.
- **Service Charges and Reimbursements**. The sharp drop between 2022 and 2023 is due to the Mercer mega-block sale, which increased the 2022 revenue by $60 million.
- **Licenses, Permits, Interest Income and Other**. The two largest sources behind the increase in this category are the interest earnings on cash and business license fees. A large amount of payments for business license renewals made in 2022 were only receipted in 2023 due to system issues, shifting some revenue between the two years.
- **Payroll Tax.** Revenues in this category declined since it only includes late payments and refunds for 2021 obligations - starting with 2022 obligations payroll expense tax revenues are being deposited into JumpStart Fund rather than General Fund.

3. Select Non-General Fund Revenue Sources

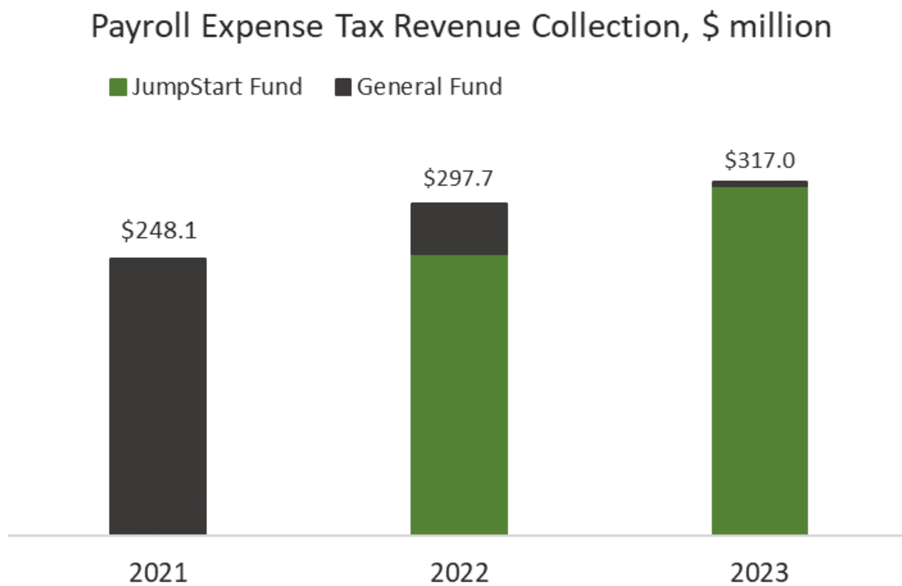
In addition to its work in forecasting and tracking the full range of GF revenues, the Forecast Office also closely tracks a select group of non-GF sources. Sections 3.1 and 3.2 present detailed discussion and analysis of the two largest non-GF sources that fall within the Forecast Office's purview;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

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. Starting with 2022 obligations, Payroll Expense Tax receipts were shifted out of the General Fund into their own separate fund, but all revenues related to 2021 obligations are still being deposited into the General Fund, no matter when they are received.

Payroll expense tax is paid by less than 500 companies and is highly concentrated at the top. Top 100 companies account for more than 90% of the tax revenue collected. About 70% of the revenues is generated from just ten companies, with eight of these ten companies operating in the tech sector. This concentration creates significant inherent volatility in this revenue stream. Changes in the financial fortunes and decisions made by a handful of individual companies can materially affect overall revenues. In particular, after experiencing a staggering growth during the pandemic, the 2021 payroll expense tax revenues significantly exceeded the forecast. In the following year, the technology sector began to cool considerably in 2022 and total payroll tax obligations declined. All largest companies laid off employees and their stock values declined. The latter is important because for many employees the total compensation subject to the tax includes the value of annual stock grants, and that part of compensation was in decline. As the tech sector stabilized in 2023 and stock prices resumed to grow, payroll expense tax obligations recovered as well.

When the accrual process for 2021 revenues was finalized in March 2022, payments for 2021 obligations totaled $248.1 million. An additional $44.5 million in late payments were received over the remainder of 2022 and became 2022 General Fund revenues. Thus, while the payments for 2022 obligations into JumpStart Payroll Expense Tax Fund were just $253.1 million, total revenue collection was $297.7 million. This also means that while in 2022 tax obligations *declined* about $39.6 million, tax collection actually *grew* by $49.5 million. In 2023, there were still some late payments made for 2021 obligations, about $3.6 million in total. As noted above, these late payments are still being deposited into the General Fund. The $313.3 million collected in 2023 for 2022 and 2023 obligations, deposited into JumpStart Payroll Expense Tax Fund, is $44.6 million or 16.6% more than the forecast from October 2023.

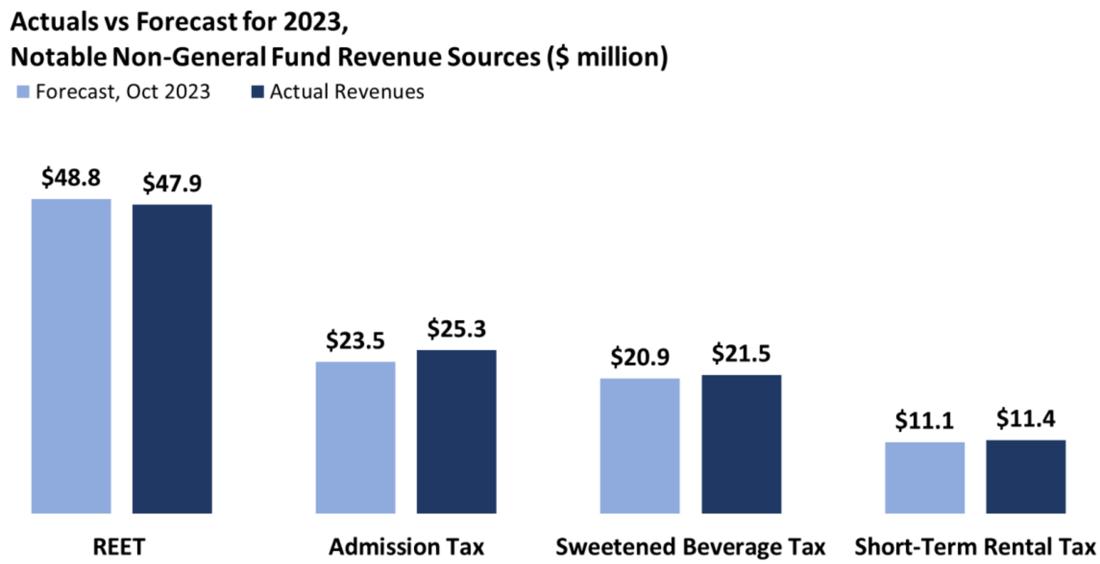


3.2 Real Estate Excise Tax (REET)

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.

REET generated a record $112 million in 2021, revenues however declined considerably since then, dropping by 47.6% year-over-year in 2023, after falling 18.5% a year before that. Interest rates increased dramatically since summer 2022, cooling both the supply and the demand side of the real estate market and resulting in fewer property sales. On the commercial real estate side, uncertainty about the long-term impact of work-from-home decreased office space values, further reducing revenue from any sale of this class of properties.

Ultimately, 2023 revenues fell $0.9 million or 1.9% short of the October forecast, reaching a final total of $47.9 million.

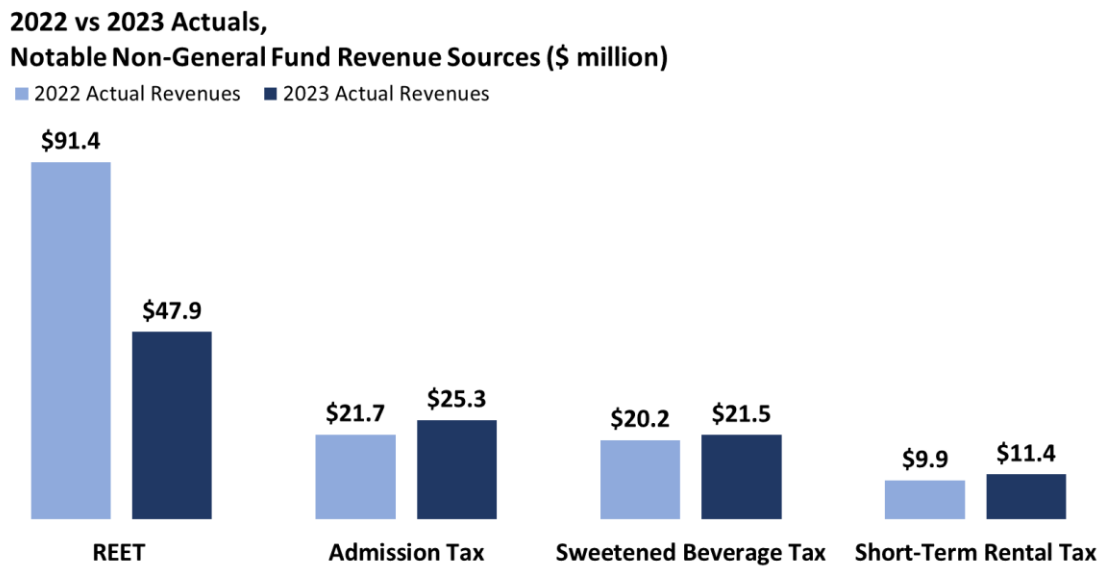


3.3 General Government Non-GF Revenues

The results presented in this subsection focus on three non-GF revenue sources 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 above compares the 2023 year-end results for each to the final October forecasts.

- Admissions tax revenue outpaced our forecast, producing an additional $1.8 million in revenue.
- Revenues from the Sweetened Beverage tax outperformed the forecast by about $0.6 million.
- Short-Term Rental Tax revenues exceeded forecasts, but by just $0.3 million.

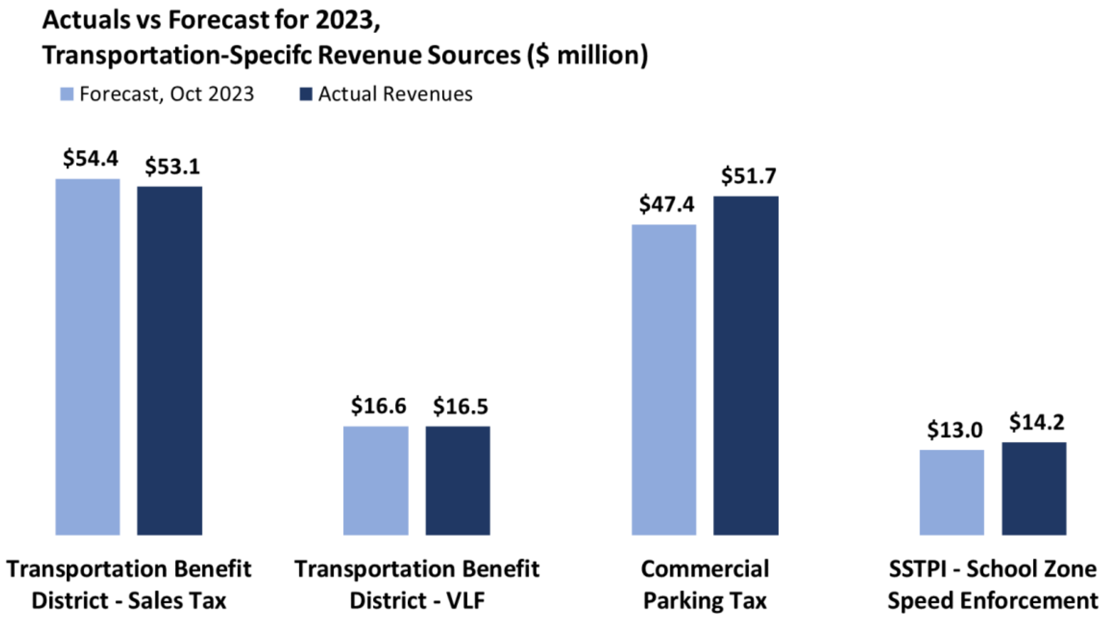
Given the impacts on large entertainment events (Admissions Tax), restaurant activity (Sweetened Beverage Tax), and tourist travel (Short-term Rental Tax), these sources had been significantly negatively impacted by the pandemic and continue to recover at different rates.



- The increase in Admissions Tax and Short-term Rental Tax revenue can be attributed to consumer spending returning back to pre-pandemic patterns and the resulting shift in spending from goods to travel and experiences, combined with the big impacts from the eventful year. In 2023, the cruise ship season saw a record breaking 1.78 million revenue passengers, Seattle hosted the Major League Baseball All-Star Week, Taylor Swift and Beyoncé concerts, and Seattle Kraken accomplished a run of play-off games.
- Sweetened Beverage Tax revenues increased by $1.3 million relative to 2022. Receipts for 2022 and 2023 were comparable through the 3rd quarter. The $1.3 million difference is entirely due to 4th quarter 2023 revenues exceeding 2022 revenue.

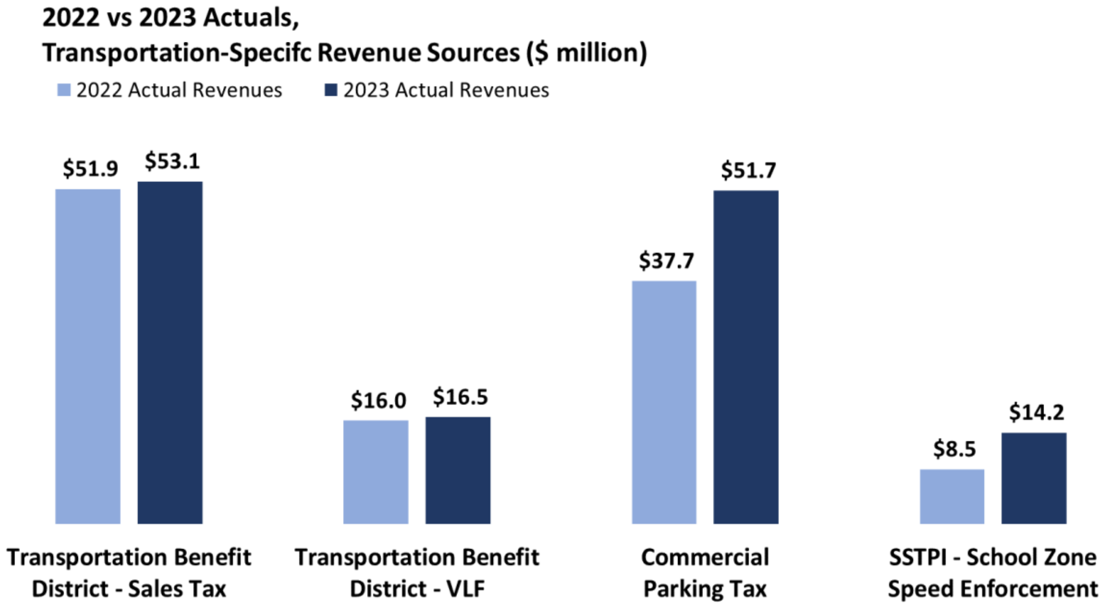
3.4 Transportation-Specific Non-GF Revenues

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 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 above, both have generated revenues below the forecast, with the Sales Tax underperforming by $1.3 million and the VLF by about $0.1 million. Same factors as those outlined in the GF section above for regular sales tax were behind the lackluster performance of the STBD sales tax.
- Commercial Parking Tax revenues, which are also dedicated to transportation purposes, far exceeded the expectations from to the October forecast, producing $4.3 million or 9.1% more than expected. $1.6 million of this difference is due to higher than expected parking activity. The rest of the $2.7 million excess is a result of a refinement of the year-end accrual method to capture more late payments and should be seen as a one-time jump in revenue.
- School zone speed enforcement camera revenues, which fund school safety transportation projects, exceeded the forecast of $11.4 million by approximately $1.2 million or 10.6%. The school safety fund also receives 20% of red-light traffic camera fine proceeds. Transferred fine receipts totaled $1.5 million against a forecast of $1.52 million.

The chart below compares the 2023 final revenues from each of these sources with revenues in the previous year.

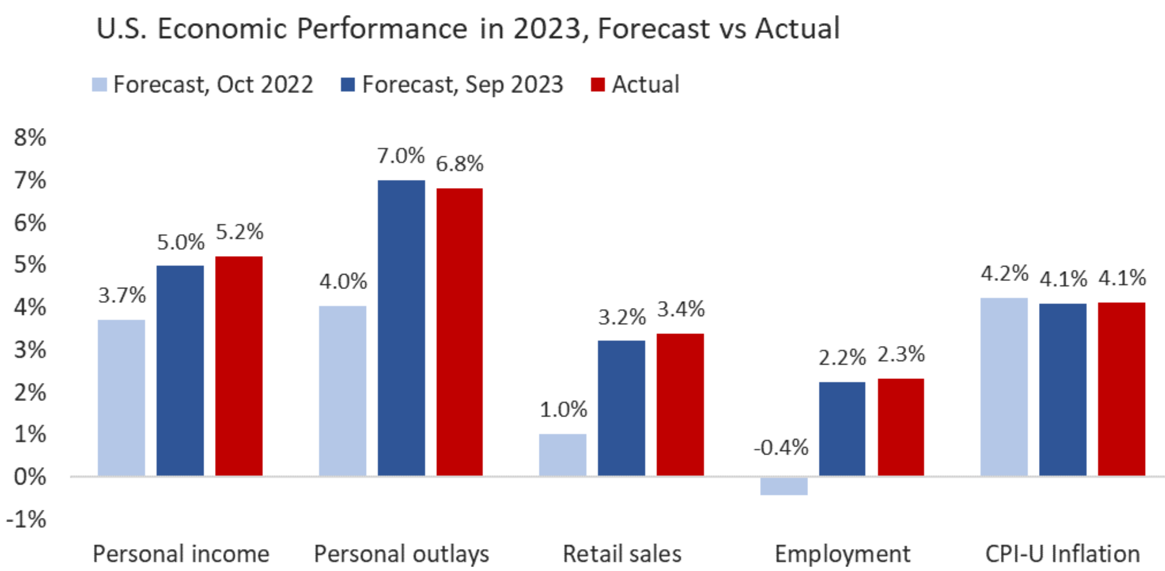


- The growth in STBD sales tax revenues was a modest 2.3% increase, notably below the 5.7% inflation rate.
- As noted above, the accrual method for the Commercial Parking Tax was revised. In addition, the tax rate increased from 12.5% to 14.5% in July 2022, which means that 2023 was the first year when the higher rates were in place the entire year. Combined with greater driving activity as employees return to the office, this led to a considerable increase year-over-year.
- Revenues from school-zone and red light cameras increased considerably from 2022. A major factor behind this large change is a backlog of incidents that were not properly reviewed in 2022, resulting in fewer paid citations. As mentioned in Court Fines above, revenues increased in 2023 due to tickets again being referred to collections in 2023. Additionally, there were 4 new cameras activated in the fall of 2022. These cameras were active for the full year in 2023 versus only a partial year in 2022.

4. Overview of Economic Climate

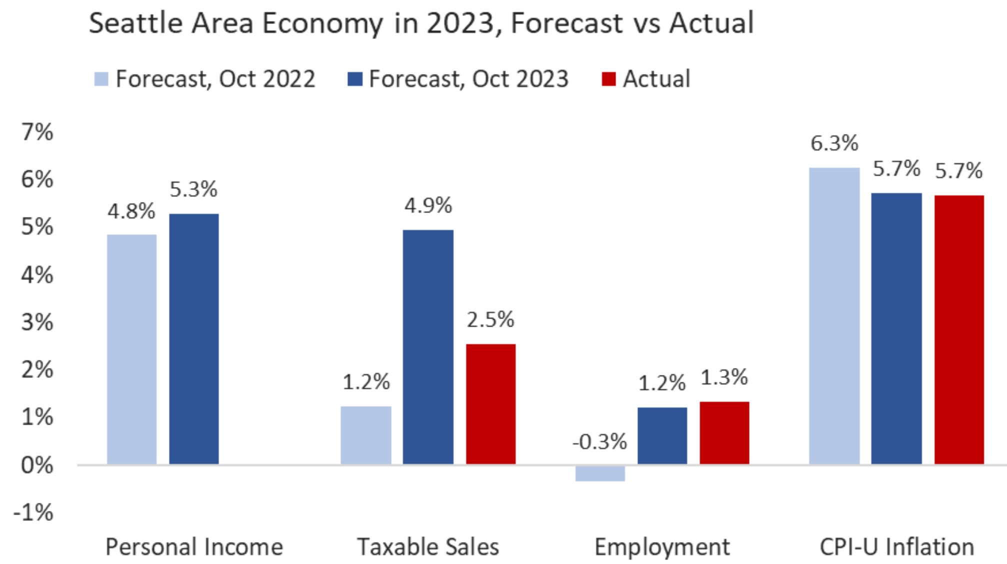
To provide some additional context for the revenue results presented in this report, this final section provides an overview of recent economic developments, with a specific focus on how conditions have evolved since the forecast for 2023 Adopted Budget was developed in October 2022.

Focusing first on the national economy, the chart below compares the forecasts of some of the key economic indicators provided by S&P Global that serve as inputs to the Forecast Office's regional economic model. Thus, their actual performance relative to forecast can help explain a part of the divergence between predicted and actual revenues.



- Despite increased uncertainty and the highly elevated risk of a recession as the economy entered 2023, the labor market and consumer spending have been much more resilient than expected. As a result, the U.S. economy avoided a recession in 2023 and instead grew at a very solid pace.
- The aggressive monetary policy tightening by the Federal Reserve Bank brought inflation down, tough it still remains uncomfortably high and above Fed's target.

A comparable assessment of our forecasts of key regional metrics reveals somewhat similar results. Final year-end results show that the regional economy outperformed our October 2022 forecast for the 2023 Adopted Budget in terms of taxable sales, but the extent of this improvement did not match our expectations as of October 2023. Hiring slowdowns and layoffs in the local technology sector led to slower regional employment growth in 2023 compared to the national economy.



- Regional personal income data is released with a significant lag and first estimates of actual 2023 personal income will only be available in November 2024.
- Taxable Sales grew faster than the dire 1.2% prediction from October 2022, but below the October 2023 prediction of 4.9%. At 2.5%, the actuals for 2023 mean that the gradual improvements in national forecasts over 2023 did not carry over completely to the sales tax revenue collected in Seattle, as consumer spending in the city was weaker than in national economy. Moreover, the downturn in the construction sector which we expected to begin in 2024, began earlier than anticipated, already in the second half of 2023, thus reducing 2023 sales tax revenue compared to our forecast.
- Regional employment outperformed expectations from the October 2022 forecast, growing 1.3% instead of declining 0.3%. This is due to continued resilience within the labor market, as healthy growth in Manufacturing, Educational and Health Services, and in Leisure and Hospitality sectors more than offset the local tech layoffs and the decline in employment in Information, Financial Activities, and in Professional and Business Services sectors. Regional employment growth was however notably weaker than in the national economy.
- While the regional inflation remained much higher than at the national level, its deceleration was faster than expected in Fall 2022. In the end, Seattle MSA CPI-U was about 0.6% lower than 6.3% forecast from October 2022 and in line with the forecast from October 2023.