

Schedule of Audit Findings and Responses

Whatcom County Whatcom January 1, 2008 through December 31, 2008

1. **Whatcom County did not comply with state law when it transferred interest earned from certain funds in which interest cannot be diverted to the general fund.**

Description of Condition

The County earned \$4,332,622 in investment interest during fiscal year 2008. The interest income was allocated as follows: \$4,236,334 to the General Fund, \$21,709 to the Veterans Relief Fund, \$1,530 to the Whatcom County Court Improvement Fund, \$35,404 to the Whatcom County Drug Fund and \$37,645 to the Ferry System Fund. During our review we noted seven funds restricted by law that did not receive interest they were due. Interest earned on funds, which are restricted, cannot be diverted to the General Fund.

The following funds are restricted and did not receive any interest allocation. We estimated the amount of interest due the funds by calculating their ending fund balance using a 3 percent return. This percentage is slightly lower than the Treasurer's estimated average return, making the calculation more conservative to better reflect the monthly fluctuation in fund balance.

Fund Name	Amount
Whatcom County Jail	\$129,859
Real Estate Excise Tax I	\$116,978
Real Estate Excise Tax II	\$274,597
Convention Center (hotel/motel tax)	\$ 20,779
Conservation Futures	\$ 73,912
Equipment Rental	\$299,353
Emergency Communication	\$ 1,928
Total	\$917,406

Cause of Condition

The County believed the restricted fund interest could be used for general government purposes rather than following the guidance in the *Budgeting, Accounting and Reporting System* (BARS) Manual based on its attorney's interpretation of the law.

Effect of Condition

When restricted revenue is used for unallowable purposes, taxpayers do not receive the intended benefit from the restricted revenue stream.

Recommendation

We recommend the County ensure interest earned in restricted funds is used for purposes allowed by law. We further recommend the General Fund reimburse the restricted funds their portion of interest earned.

County's Response

EXECUTIVE SUMMARY OF WHATCOM COUNTY'S RESPONSE TO THE STATE AUDIT TEAM'S FINDING REGARDING INTEREST INCOME

1. *The audit team finding misstates the law and the content of the SAO BARS Manual matrix in its claim that interest earned on funds which are restricted cannot be diverted to the General Fund. The matrix specifically allows for applying interest income from investment of restricted funds to general fund uses for over 20 of those restricted funds.*
2. *There are several areas upon which Whatcom County and the SAO generally agree, and recognizing that helps to better focus the reason for the disagreement.*
3. *RCW 36.29.020 establishes the general principle that interest income from restricted funds can be used for general fund purposes in the absence of direction to the contrary. The direction provided by the Whatcom County Council through the adoption of ordinances which assign usage of the interest income consistent with the County's interpretation of state law is based squarely on this principle.*
4. *Washington's State Legislature knows how to provide clear direction to municipalities when it intends that interest income be used strictly for the benefit of the restricted fund. It has done so with admirable clarity on three occasions widely separated in time, and with regard to funds for quite different purposes. That it did not provide prohibitory language with regard to the funds in question here is strong indication that there is no such restriction upon interest income from investment of those funds.*
5. *It is helpful to review the process that has yielded the audit team's finding, so that the lengthy effort of the County and others to correct the SAO's statutory misinterpretation that underlies the BARS Manual matrix is not overlooked, and so that the intensely human component of statutory interpretation is recognized.*
6. *The Asst. AGs performed unsound statutory analysis and ignored the most applicable maxim of statutory construction when they advised the SAO on the content of its BARS Manual matrix.*
7. *The distinction that the SAO's BARS Manual matrix draws between "moneys collected" and "moneys received" and the meaning it assigns to that distinction is erroneous in light of the context in which those terms are used. (for the first and seventh of the seven statutes for which non-compliance is alleged).*
8. *To broadly interpret the statutory meaning of "revenue(s)" apart from the words that immediately follow it within the statutes ("from the tax imposed"), is once*

again a failure to apply one of the most rudimentary principles of statutory construction, **noscitur a sociis**. (for the second, third, and fourth of the seven allegedly violated statutes)

9. For the remaining two restricted funds, the audit team's findings are based upon one logical fallacy known in Latin as **petitio principii**, but known more commonly to us as "begging the question." (for the fifth and sixth of the seven allegedly violated statutes)
 - a. RCW 84.34.240(1) first notes that taxes collected from the property tax levy for conservation futures may be credited to the conservation futures fund, and then notes that amounts placed into the fund must be used for that restricted purpose. It does not address the question of investment or whether the interest income from investment of the principal is to be placed into the conservation futures fund.
 - b. Moneys "accumulated" in the equipment rental and revolving fund are those sums of money deposited into the fund pursuant to RCW 36.33A.050, and do not include interest income from investment of the principal balance, inasmuch as that interest income is never deposited into the ER&R fund.
10. The SAO's proposed finding of violation against Whatcom County pertaining to the application and use of interest income should be stricken and the BARS Manual matrix should be modified to correct the identified errors.

The full argument in support of these points in the executive summary is contained in the following 13-page document, together with its various exhibits. Whatcom County recommends reading the full document carefully to better understand and appreciate the nature of the County's argument in support of its conclusions.

Noscitur a sociis: a legal maxim indicating that the meaning of an unclear word or phrase is to be determined (constructed) on the basis of its context, with reference to the words or phrases surrounding it. As UK judge J. Stamp put it (in the 1967 case of *Bourne vs. Norwich Crematorium Ltd.*), "Sentences are not mere collections of words to be taken out of the sentence, defined separately by reference to the dictionary or decided cases, and then put back into the sentence with the meaning you have assigned to them as separate words . . ." The maxim itself is the Latin phrase literally interpreted "it is known by the company it keeps."

On September 21, upon completion of its annual audit, the regional audit team of the State Auditor's Office issued to Whatcom County its draft Schedule of Audit Findings and Responses. Its first finding declared that "Whatcom County did not comply with state law on the use of restricted fund interest." In the ensuing Description of Condition, the audit team claimed that "Interest earned on funds which are restricted cannot be diverted to the General Fund." In the Effect of Condition section, the audit team claimed that "When restricted revenues are used for unallowable purposes, taxpayers do not receive the intended benefit from the restricted revenue stream." This characterization of what Whatcom County has done is misinformed and calls for a response.

1. The audit team finding misstates the law and the content of the SAO BARS Manual matrix¹ in its claim that interest earned on funds which are restricted cannot be diverted to the General Fund.

The audit team's assertion that interest earned on restricted funds cannot be diverted to the General Fund is a significant misstatement of the law and of the real issue in this case. This is demonstrated by the BARS Manual guidance to which the audit team refers in its finding and that it urges the County to follow. The State Auditor's Office has indeed issued "guidelines" on this matter of the allocation of interest income and it must be recognized that the entire list of funds addressed in its BARS manual matrix is comprised of "restricted funds," that is, funds which may be used for a restricted purpose only. For a significant number of those restricted funds the SAO said interest income can be applied to the general fund, and for others on the list of restricted funds it said that interest income must be returned for the use of the restricted fund only and could not be applied elsewhere. In fact, Whatcom County counts 21 restricted funds (out of a total of 47) on the BARS manual matrix for which the SAO states that interest income can be used for general fund purposes. Thus it is erroneous and substantially misleading to state without qualification, as the audit team does, that interest earned on restricted funds cannot be diverted to the General Fund. By the SAO's own guidance, the interest from restricted funds may or may not be applied to the general fund, depending on the language of the statute pertaining to the particular restricted fund.

2. It is helpful to review the areas upon which Whatcom County and the SAO generally agree in order to better understand the essence of the disagreement.

Whatcom County agrees with the SAO that money in restricted funds must be used solely for the purpose for which the restricted fund was established. Whatcom County has acted consistently with that principle and the SAO has made no claim to the contrary with regard to the principal balance of those seven restricted funds at issue here. No tax revenues placed in any of these restricted funds have been diverted to the general fund. The question at hand pertains to the use of interest income resulting from the investment of those funds. Next, Whatcom County generally agrees with the SAO that interest income from some funds is indeed restricted to use within those restricted funds, while interest income from other restricted funds can be deposited in the general fund and used for general fund purposes. Whatcom County agrees with the SAO that interest income from (at least) 21 restricted funds can be used for general funds purposes. Whatcom County further identifies three restricted funds to which interest income must be applied, pursuant to the plain language of the pertinent statutes. The real issue here is whether interest income from investment of money in the remaining restricted funds can be used for general fund purposes, or if it must be added to the balance of funds within the restricted account for use in that fund only. The BARS Manual purports to distinguish between the various restricted funds in this matter, with 21 "yes" and 26 "no" designations on the issue of interest income diversion to the general fund. Whatcom County agrees

¹ We believe the correct reference for this matrix is State Auditor Interpretation #22, found at Vol. 1, Part 3, Chapter 12, p. 42 of the 2008 BARS Manual, and that the matrix was first promulgated in the 2007 BARS Manual update.

with the SAO on 24 of the 47 matrix designations, with 21 on the “yes” end and 3 on the “no” end. We disagree with 23 designations that lie between those agreed “yes’s” and “no’s”, seven of which are at issue here.

- 3. Whatcom County believes that RCW 36.29.020 establishes the general principle that interest income from restricted funds can be used for general fund purposes in the absence of direction to the contrary.**

So how do we determine whether those 23 disputed funds (including the seven in issue here) lie properly in the “yes” column or the “no” column as it pertains to the use of interest income for the general fund? Here again, we agree with the SAO that the statutory language is determinative. Because RCW 36.29.020 allows the County Treasurer to apply interest income from investment of restricted funds to general funds purposes in a general sense², Whatcom County operates from the principle that the appropriate default position is to allow investment income from restricted funds to be used for general fund purposes unless particular statutes direct otherwise. That is, the general statute establishes the background principle that allows application of interest income to the general fund, but that general statute can certainly be trumped by a particular statute that directs the opposite result. This principle is effectuated by direction provided within ordinances adopted by the Whatcom County Council.

- 4. Washington’s State Legislature knows how to provide clear direction to municipalities when it intends that interest income be used strictly for the benefit of the restricted fund. It has done so with admirable clarity on three occasions widely separated in time, and with regard to funds for quite different purposes.**

Whatcom County has identified three restricted funds for which the pertinent statutes direct interest income back to the restricted funds, with the particular statute trumping the general statute. Those three are the funds for the Fire Insurance Premium tax (RCW 41.16.050, .060), the Veterans’ Assistance tax (RCW 73.08.080), and the High Occupancy Vehicle System tax (RCW 81.100.060, .080). Following is the language of the statutes for each of those three funds.

Firefighters’ Pension Fund:

There is hereby created and established in the treasury of each municipality a fund which shall be known and designated as the firefighters' pension fund, which shall consist of: (1) All bequests, fees, gifts, emoluments, or donations given or paid thereto; (2) twenty-five percent of all moneys received by the state

² The pertinent language of RCW 36.29.020 is: “Whenever the funds of any municipal corporation which are not required for immediate expenditure are in the custody or control of the county treasurer, and the governing body of such municipal corporation has not taken any action pertaining to the investment of any such funds, the county finance committee shall direct the county treasurer . . . to invest . . . such funds The interest or other earnings from such investments or deposits shall be deposited in the current expense fund of the county and may be used for general county purposes. . . .” In this particular case, the Whatcom County Treasurer was investing and allocating the funds in question pursuant to the requirements of state law and of County ordinance by which the County Council, consistent with state law, directed the manner in which the interest income was to be applied to the use of the various funds.

from taxes on fire insurance premiums; (3) taxes paid pursuant to the provisions of RCW 41.16.060; **(4) interest on the investments of the fund**; and (5) contributions by firefighters as provided for herein. The moneys received from the tax on fire insurance premiums under the provisions of this chapter shall be distributed in the proportion that the number of paid firefighters in the city, town, or fire protection district bears to the total number of paid firefighters throughout the state . . . **RCW 41.16.050**, pertinent language in effect since at least 1947.

Veterans' Assistance Fund:

- (1) The legislative authority in each county shall levy, in addition to the taxes now levied by law, a tax in a sum equal to the amount which would be raised by not less than one and one-eighth cents per thousand dollars of assessed value, and not greater than twenty-seven cents per thousand dollars of assessed value against the taxable property of their respective counties, to be levied and collected as now prescribed by law for the assessment and collection of taxes, for the purpose of creating a veterans' assistance fund. Expenditures from the veterans' assistance fund, **and interest earned on balances from the fund**, may be used only for:
 - (a) The veterans' assistance programs authorized by RCW 73.08.010;
 - (b) The burial or cremation of a deceased indigent veteran or deceased family member of an indigent veteran as authorized by RCW 73.08.070; and
 - (c) The direct and indirect costs incurred in the administration of the fund as authorized by subsection (2) of this section. **RCW 73.08.080 (1)**, pertinent language added in 2005.

High Occupancy Vehicle System Fund:

- (1) Funds collected under RCW 81.100.030 or 81.100.060 **and any investment earnings accruing thereon** shall be used by the county or the regional transportation investment district in a manner consistent with the regional transportation plan only for costs of collection, costs of preparing, adopting, and enforcing agreements under RCW 81.100.030(3), for construction of high occupancy vehicle lanes and related facilities, mitigation of environmental concerns that result from construction or use of high occupancy vehicle lanes and related facilities, payment of principal and interest on bonds issued for the purposes of this section, for high occupancy vehicle programs as defined in RCW 81.100.020(5), or for commuter rail projects in accordance with RCW 81.104.120.

RCW 81.100.080 (1), pertinent language adopted in 1990.

These three examples demonstrate that the State Legislature knows how to provide clear direction to municipalities when it desires that interest income earned from investment of restricted funds be applied to the benefit of that particular fund instead of the general fund. It has done so in these three instances with language that is simple, direct, and conclusive. It has done so at three significantly different points in time which bracket the adoption of the statutes considered below. If the legislature wants to impose a restriction on the use of interest income from a restricted fund, it will do so with language akin to what we find in these three statutes. The map laid out by the legislature here points clearly to the path of compliance. This is not a sketchy map where municipalities are left to guess or argue with the SAO where the path lies. Whatcom County fully agrees that the particular statutes cited above trump the general principle laid out in RCW 36.29.020.

- 5. It is helpful to review the process that has yielded the audit team's finding, so that the lengthy effort of the County and others to correct the SAO's statutory misinterpretation that underlies the BARS Manual matrix is not overlooked, and so that the intensely human component of statutory interpretation is recognized.**

In light of the clear language cited above, what language did the legislature use for the 23 funds that the SAO and Whatcom County dispute, and how should that language be construed? Before we try to follow the footsteps of the SAO into the thicket of its statutory (mis)construction, we should stop, take a breath, and identify the players. To directly address differences of opinion with the SAO on this very topic, the Whatcom County Treasurer, several other county treasurers, staff from the Washington Association of County Officials (WACO), and the Assistant Chief Civil Deputy of the Whatcom County Prosecutor's Office met with staff from the State Auditor's Office on a couple of occasions within the last year. In addition, there were at least two telephone conversations between the above-referenced civil deputy from the Whatcom County Prosecutor's Office and an assistant attorney general. In the second of the two phone conversations, there were two assistant AGs on the line. In the initial phone conversation (late summer 2008), the Asst. AG indicated that she stood behind the matrix generated by the SAO but that she had not done the analysis herself so was not prepared at that point to explain the rationale for its conclusions. The need for her to look into the issue more deeply was understandable. During the second phone conversation, on April 7, 2009, she and another Asst. AG defended the matrix based upon what they believed were material distinctions between the various statutes establishing the numerous restricted funds. When asked to provide the reasons for the conclusions they were defending, they responded that there was a lot of money involved and that they used dictionary definitions of terms that they believed were unclear in their effort to ascertain a more precise meaning of the statutes in question. These same two Asst. AGs were physically present for a second meeting between SAO staff, several county treasurers, WACO staff, and the Asst. Chief Civil Deputy of the Whatcom County Prosecutor's Office, which occurred in May 2009 at the SAO's offices in Olympia. There the parties reiterated their positions and discussed what it would take to resolve their differences over what constituted the proper interpretation of the statutory language in question. The Asst. AGs re-emphasized their use of

dictionary definitions of such terms as “proceeds”, “revenue”, and “received”. They were evidently not persuaded by the deputy prosecutor’s counter-argument that the context in which those terms were used provided sufficient indication of their meaning. It was obvious at that point that the SAO was directing regional audit teams to make this matter the subject of the annual county audits this year and that audit findings would be issued to counties who applied a different interpretation than the SAO.

6. The Asst. AGs performed unsound statutory analysis and ignored the most applicable maxim of statutory construction when they advised the SAO on the content of its BARS Manual matrix.

Returning from that review of the players involved in this dispute, what is the particular language in dispute and how does the SAO assign such a meaning to it that it asserts, not merely disagreement with Whatcom County’s interpretation, but that Whatcom County is out of compliance with state law? In contrast to the clear language of the three statutes cited above (which direct interest income back to the restricted fund), the language used in the statutes, the meaning of which is in dispute, lays out no clear path, or at least not the path that the Asst. AGs and the SAO have created. The Asst. AGs have tried to blaze a trail where none exists, attaching great significance to what they believe are trail markers. However, those particular markers lead them ultimately in a self-contradictory circle. The path that the Asst. AGs and the SAO demand that we follow is one that they hacked out on the basis of distinctions without differences, supposed differences in meaning between “money collected” and “money received”, and an insistence that “revenues from the tax imposed” means “government income from all sources”. Their reliance upon dictionary definitions of terms considered in isolation rather than context is a stark example of fallacious statutory interpretation condemned by the judge quoted at the outset of the County’s response: **“Sentences are not mere collections of words to be taken out of the sentence, defined separately by reference to the dictionary or decided cases, and then put back into the sentence with the meaning you have assigned to them as separate words . . .”** The applicable maxim of statutory interpretation that lends clarity and yields correct interpretation in this case is **noscitur a sociis**, which rendered literally means “it is known by the company it keeps”. In reference to words and their interpretation, it directs us to closely consider the context in which words are used in order to ascertain their proper meaning.

The seven statutes cited by the audit team, which it claims that Whatcom County has misinterpreted and misapplied, provide a good avenue of insight into the differences in interpretation between the two parties.

7. The distinction that the SAO’s BARS Manual matrix draws between “moneys collected” and “moneys received” and the meaning it assigns to that distinction is erroneous in light of the context in which those terms are used.

The first statute cited by the audit team is RCW 82.14.350, regarding sales and use tax for juvenile detention facilities and jails. The operative language in the statute for the question at hand is: “(3) **Moneys received from any tax imposed under this section** shall be used solely for the purpose of providing funds for

costs associated with financing, design, acquisition, construction, equipping, operating, maintaining, remodeling, repairing, reequipping, and improvement of juvenile detention facilities and jails” (emphasis added, dlj). Exactly the same language is used in the seventh statute which the audit team accused the County of violating, RCW 82.14.420, so we will consider these two alleged violations together. A closer look at the BARS Manual matrix constructed by the SAO helps us to focus our consideration even more closely, upon the word “**received**”, as the basis for the SAO’s conclusion. How do we know this is the critical word in the Asst. AGs’ and SAO’s opinion? When they looked at another statute, RCW 82.14.460(3) (pertaining to sales and use tax for chemical dependency or mental treatment services), and interpreted the following language: “Moneys **collected** under this section shall be used solely for the purpose of providing for the operation or delivery of new or expanded chemical dependency or mental health treatment . . .”, they reached the opposite conclusion, that interest income in that instance could be applied to general fund uses. The use of the two different verbs, “received” and “collected” is the sole difference between the operative language of the two statutes. Why, in the reasoning of the Asst. AGs and the SAO, is the difference between “received” and “collected” dispositive? Because, they argue, “collected” limits the funds in issue to those arising at the point of the imposition of the tax and thus does not extend to the interest income from investment of those funds, whereas “received” expands the funds in issue to include those earned from investment of the taxes collected.

But does this difference between “collected” and “received” actually bear the heavy freight that the SAO’s matrix places upon it? No. When the Asst. AGs and the SAO analyze yet another statute, RCW 82.45.180(3), they encounter the verb “received” but reach the opposite conclusion that they did for RCW 82.14.350. There, in reference to the funds collected through the imposition of a real estate excise tax electronic technology fee, the legislature said: “(c) When **received** by the county treasurer, the funds shall be placed in a special real estate excise tax electronic technology fund held by the county treasurer to be used exclusively for the development, implementation, and maintenance of an electronic processing and reporting system for real estate excise tax affidavits.” It is instructive to note in regard to this last statute that the SAO first said that the interest income resulting from investment of those funds must be used strictly for the benefit of that fund, but subsequently reversed itself (effective January 1, 2008) and indicated that interest income from that restricted fund could be used for general fund purposes. By virtue of the language surrounding the verb “received” in RCW 82.45.180(3), it must have become obvious to the SAO that its prior broad interpretation of “received” was not applicable in this situation. The verb “received” here refers to what occurs in the process of distribution of excise taxes from the state to the counties (state “collects” and distributes to the county, which therefore “receives” the money from the state) and has nothing to do with the receipt of money from whatever source, which had been the rationale for the earlier distinction between “received” and “collected”. However, upon fuller consideration of the context in which the verb “received” is used throughout these various statutes, it becomes obvious that RCW 82.45.180(3) simply makes clearer what is also true of every other instance in which the verb “received” is used: invariably it is used within the context of a distribution of funds from the state to counties or other municipalities. “Received” as used in all of these statutes does not bear the meaning sometimes assigned to it by the Asst. AGs and the SAO, that is, money from whatever source, but always occurs in a

context marked by the municipalities' receipt of funds upon distribution of revenue from the state. The fact that the legislature sometimes used the term "collected" in this same context only goes to prove that the difference between the two verbs is inconsequential in regard to what the legislature intended, and thus has no bearing whatsoever on the issue of how to apply interest income. This example of how the Asst. AGs advising the SAO saw the same marker ("received") repeatedly and came to opposite conclusions of its meaning is a demonstration of how they got off the trail and instead of recognizing they were lost, contradicted themselves to make sense of what they thought they were seeing.

The County also notes that, in line with its next point of analysis, the words "moneys received" are immediately followed by the words "from the tax imposed" which clarifies that the money to which the legislature makes reference in these statutes is not money from interest income but money from taxation.

8. **To broadly interpret the statutory meaning of "revenue(s)" apart from the words that immediately follow it within the statutes ("from the tax imposed"), is once again a failure to apply one of the most rudimentary principles of statutory construction, noscitur a sociis.**

The same type of linguistic imprecision critiqued above is evident in the SAO's interpretation of the term "revenue from the tax imposed" and its various functional equivalents. The following terms are used in the second, third, and fourth statutes with which the County is accused of being out of compliance:

"Revenues generated from the tax imposed . . . shall be used . . . solely for financing capital projects . . ." RCW 82.46.035(3).

". . . revenues generated from the tax imposed . . . shall be used solely for financing capital projects . . ." RCW 82.46.010(2).

". . . all revenue from taxes imposed under this chapter shall be credited to a special fund in the treasury of the municipality imposing such tax and used solely for the purpose of paying all or any part of the cost of tourism promotion, acquisition of tourism-related facilities, or operation of tourism-related facilities." RCW 67.28.1815.

In each of the cited statutes, the common and operative language is "revenue(s) from tax(es) imposed." Here, rather than judge the meaning of the words by their context, the Asst. AGs reach for the dictionary and end up straying well off the path. On a 2-sheet handout provided to Whatcom County by the Asst. AGs and the SAO, they reprinted the Webster's II New College Dictionary definition of revenue and concluded that it here meant government income from all sources, including interest income. As far as they were concerned, that concluded the argument. They did the same with the word "proceeds". However, when one inserts their expanded definition into the sentence in which the original word is found, one ends up with this tortured phrase: "all government income from whatever sources from the tax imposed shall be used solely for [the designated purpose] . . .", which is a rather nonsensical reading. The statutes already tell us

precisely what government income is the object of concern here: it is the government income from the tax imposed. We need not guess at the source of the government income and speculate that it includes subsequent investment income, since the source has been clearly identified. To dig more deeply, “tax” as used in each of these three statutes refers to the imposition of a particular sort of governmental charge. The yield of that imposition is identified here as the revenue in question. The statutes do not read: “the revenue from the revenue from the tax(es) imposed”. Rather the revenue is specifically identified as that revenue from the imposition of the tax in question. If the word “tax” had been used in this context as synonymous with the money that results from taxation (as in “I paid my taxes”), then the SAO’s conclusion would have more purchase. But as noted, in each of these instances “tax” is used to denote the imposition itself, and therefore “revenue” as used here is the yield of that imposition, not the yield of the investment of the money obtained by the imposition.

Returning to the argument regarding contextual meaning, the term “revenue” is specifically modified by the prepositional phrase immediately following it in the statutes in question (“from the tax imposed”) to signify the income generated at the point of taxation. In light of that grammatical construct, it is erroneous to use a more general definition of revenue to trump a more specific meaning that is already supplied by the context. The same argument applies with equal force to the term “proceeds.” When the Asst. AGs and the SAO offer a Webster’s Dictionary definition of “proceeds” that means “money obtained from a commercial or fun-raising [sic] venture,” that dictionary definition is obviously not talking about tax proceeds. “Proceeds” has a much more limited meaning when used in the various taxing statutes than that supplied by the general dictionary definition. In fact, RCW 82.45.180 (1) (b) (iii) provides a statutory definition of “proceeds”: “moneys collected and receipted by the county from the taxes imposed by this chapter, less the county’s share of the proceeds used to defray the county’s costs of collection allowable . . .” In their use of broad dictionary definitions the Asst. AGs completely overlooked *noscitur a sociis*, the elementary maxim of statutory construction pertaining to context that we cited above and have discussed and applied at length.

9. **For the remaining two restricted funds, the audit team’s findings are based upon one logical fallacy known in Latin as *petitio principii*, but known more commonly to us as “begging the question.”**

In the preceding portions of the response, Whatcom County has addressed 1) the alleged violation of the first and seventh statutes together as they both are based upon the meaning of “moneys received”, and 2) the alleged violations of the second, third, and fourth statutes together as they are all based upon the meaning of “revenue(s) from the tax(es) imposed”. In this final portion of our response, the County will address together the alleged violations of the fifth (RCW 84.34.240) and sixth (RCW 36.33A.060) statutes cited by the audit team, inasmuch as the same fallacy underlies the SAO’s reasoning for those two separate statutes. In both instances, the SAO assumes that which is to be proven, that is, it assumes that the interest income that was earned was necessarily placed into the restricted fund, from which it then argues that the interest income cannot be removed from the restricted fund for general fund purposes. That initial assumption is incorrect in both cases.

- a. **RCW 84.34.240(1) first notes that taxes collected from the property tax levy for conservation futures may be credited to the conservation futures fund, and then notes that amounts placed into the fund must be used for that restricted purpose. It does not address the question of investment or whether the interest income from investment of the principal is to be placed into the conservation futures fund.**

This particular alleged violation provides us with the starkest example of how the SAO is assuming that which is to be proven. Evidently the SAO assumes that when money from the various county funds is invested, the interest income is initially credited back to that fund and is thereafter moved or “diverted” to the general fund. But from an accounting standpoint, that is not what happens. The interest income earned upon the money in the undifferentiated investment pool is allocated by the Treasurer as follows³: a proportionate share to those funds that the legislature has identified as the proper recipient of earnings from the investment of their principal, a proportionate share back to other funds which the County Council itself designates as the recipients of the income from investment of their principal even though the state legislature has not mandated that, and finally the remaining share to the general fund to be used for general fund purposes. For the conservation futures fund, there is no statutory instruction to place interest income into the conservation futures fund, so the money from interest income is never placed within that fund, and thus the limitation on the use of money placed in that fund does not apply to interest income.

- b. **Moneys “accumulated” in the equipment rental and revolving fund are those sums of money deposited into the fund pursuant to RCW 36.33A.050, and do not include interest income from investment of the principal balance, inasmuch as that interest income is never deposited into the ER&R fund.**

Again, as for the conservation futures fund, the SAO appears to assume that interest income from investment of the ER&R fund is deposited into that fund, where it accumulates along with other deposits, and thus is subject to the restriction placed upon money that accumulates within that fund. That is not how the accounting works. Rather, the moneys “accumulated in the equipment rental and revolving fund” to which reference is made in RCW 36.33A.060, are the sum of the deposits into the fund, the sources of which are identified in RCW 36.33A.050. Nowhere is interest income or other investment income identified within that statute as being the source of those deposits. Where that statute identifies the source of money as “any source lawfully available to it”, it states that the County “may” place that money in the fund. For other identified sources, the placement of that money in the fund is mandatory, but interest income is nowhere found on the mandatory list. The logical

³ As noted in footnote 1, the County Treasurer makes his allocation of interest income consistent with the requirements of state law and county ordinance. The County Council in this case has adopted ordinances which direct the use of investment income consistent with Whatcom County’s interpretation of the applicable statutes.

fallacy of **petitio principii** or “begging the question” rears its head again as in the prior alleged violation.

CONCLUSION

It has caused enough trouble that the SAO has, in its matrix, given Washington municipalities wrong directions on utilizing interest income. It is the crowning blow that the SAO’s audit team, following instructions from SAO headquarters based upon erroneous advice from Asst. AGs, is ready to declare Whatcom County out of compliance with state law because the County chooses to stay on the statutorily-defined path rather than follow the SAO into the woods.

In its numerous contacts with the Asst. AGs and the SAO regarding this issue prior to the audit team conducting its annual audit, the County urged the Asst. AGs and the SAO to put forward their best argument to justify the matrix. The SAO referred us to the Asst. AGs, and the Asst. AGs referred us to the dictionary. Whatcom County, in light of the more thorough analysis that it had conducted, was not at all convinced that the very slender reed upon which the SAO and Asst. AGs rested their case was adequate to bear that weight. The County believes with good cause that this question should not be settled by considering which agency is larger, or which one is based in Olympia, or even which one has the statutory duty to monitor the activities of the other for compliance with accountancy principles. The proper execution of the SAO’s monitoring duty is premised upon an underlying obligation to correctly interpret the applicable law, and in order to perform that task, responsible parties must base their conclusions upon a rigorous legal analysis that correctly applies the pertinent rules of statutory interpretation. That is what Whatcom County believes it has provided here. For all of the reasons given above, the draft finding of violation against Whatcom County pertaining to interest income should be stricken and the guidelines supplied in the BARS Manual matrix should be amended to reflect the proper meaning of the statutes analyzed above.

Auditor’s Remarks

We thank the County for its response to the finding. We worked with the County on several occasions regarding its use of restricted interest and its analysis of the laws and regulations. The Attorney General’s Office also reviewed and considered the County’s interpretation at various times over the last year, as well as its response to this finding. Additionally, our Office has worked with the County Association on numerous occasions in regards to this issue. We reaffirm our finding and will review the condition during our next audit.

Applicable Laws and Regulations

RCW 43.09.200 states in part:

The state auditor shall formulate, prescribe, and install a system of accounting and reporting for all local governments, which shall be uniform for every public institution, and every public office, and every public account of the same class.

The system shall exhibit true accounts and detailed statements of funds collected, received, and expended for account of the public for any purpose whatever, and by all public officers, employees, or other persons.

The accounts shall show the receipt, use, and disposition of all public property, and income, if any derived there from; all sources of public income, and the amounts due and received from each source; all receipts, vouchers, and other documents kept, or required to be kept, necessary to isolate and prove the validity of every transactions

Budgeting, Accounting and Reporting System (BARS) Manual - Part 3, Accounting, Chapter 12.22, Transfer of Interest Income to the General Fund and/or Other Funds, states in part:

Based on the current economic environment in which they operate, local governments are actively looking for ways to generate additional unrestricted revenues, so often there are questions regarding the transfer of interest income associated with certain revenues to the general fund.

The answers to the question “Can the interest earned on this revenue be deposited to the general fund or other funds?” may be yes or no, based on the statutory language that authorized the imposition of taxes and levies or the distribution of fees and taxes by the state.

SAO has reviewed the language related to various taxes, levies and fees and prepared the attached matrix to assist local governments in determining whether interest transfers made by them are allowable. The matrix shows the type of the restricted revenue, associated RCW provision and a yes or no answer on the transferability of interest.

This should not be considered an exhaustive list of all situations related to interest transfers. The matrix does not address revenues restricted by bond covenants. Additional questions about transfers of interest income generated by other types of revenue should be directed to the SAO staff.

Source of Revenue	RCW	Can the interest be diverted to general and/or other funds?
Jails	82.14.350	No
REET I	82.46.010	No
REET II	82.46.035	No
Hotel/Motel Tax	67.28.1815	No
Conservation Futures	84.34.240(1)	No
Equipment Rental	36.33A.060	No
Emergency Communication	82.14.420	No

RCW 82.14.350, Sales and use tax for juvenile detention facilities and jails – Colocation, states:

(1) A county legislative authority in a county with a population of less than one million may submit an authorizing proposition to the county voters, and if the proposition is approved by a majority of persons voting, fix and

impose a sales and use tax in accordance with the terms of this chapter for the purposes designated in subsection (3) of this section.

(2) The tax authorized in this section shall be in addition to any other taxes authorized by law and shall be collected from those persons who are taxable by the state under chapters 82.08 and 82.12 RCW upon the occurrence of any taxable event within the county. The rate of tax shall equal one-tenth of one percent of the selling price in the case of a sales tax, or value of the article used, in the case of a use tax.

(3) Moneys received from any tax imposed under this section shall be used solely for the purpose of providing funds for costs associated with financing, design, acquisition, construction, equipping, operating, maintaining, remodeling, repairing, reequipping, and improvement of juvenile detention facilities and jails.

(4) Counties are authorized to develop joint ventures to colocate juvenile detention facilities and to colocate jails.

RCW 82.46.035, Additional tax – Certain counties and cities – Ballot proposition – Use limited to capital projects – Temporary rescindment for noncompliance, states in part:

(3) Revenues generated from the tax imposed under subsection (2) of this section shall be used by such counties and cities solely for financing capital projects specified in a capital facilities plan element of a comprehensive plan. However, revenues (a) pledged by such counties and cities to debt retirement prior to March 1, 1992, may continue to be used for that purpose until the original debt for which the revenues were pledged is retired, or (b) committed prior to March 1, 1992, by such counties or cities to a project may continue to be used for that purpose until the project is completed.

(4) Revenues generated by the tax imposed by this section shall be deposited in a separate account.

RCW 82.46.010, Tax on sale of real property authorized – Proceeds dedicated to local capital projects – Additional tax authorized – Maximum rates, states:

(1) The legislative authority of any county or city shall identify in the adopted budget the capital projects funded in whole or in part from the proceeds of the tax authorized in this section, and shall indicate that such tax is intended to be in addition to other funds that may be reasonably available for such capital projects.

(2) The legislative authority of any county or any city may impose an excise tax on each sale of real property in the unincorporated areas of the county for the county tax and in the corporate limits of the city for the city tax at a rate not exceeding one-quarter of one percent of the selling price. The revenues from this tax shall be used by any city or county with a population of five thousand or less and any city or county that does not

plan under RCW 36.70A.040 for any capital purpose identified in a capital improvements plan and local capital improvements, including those listed in RCW 35.43.040.

After April 30, 1992, revenues generated from the tax imposed under this subsection in counties over five thousand population and cities over five thousand population that are required or choose to plan under RCW 36.70A.040 shall be used solely for financing capital projects specified in a capital facilities plan element of a comprehensive plan and housing relocation assistance under RCW 59.18.440 and 59.18.450. However, revenues (a) pledged by such counties and cities to debt retirement prior to April 30, 1992, may continue to be used for that purpose until the original debt for which the revenues were pledged is retired, or (b) committed prior to April 30, 1992, by such counties or cities to a project may continue to be used for that purpose until the project is completed.

(3) In lieu of imposing the tax authorized in RCW 82.14.030(2), the legislative authority of any county or any city may impose an additional excise tax on each sale of real property in the unincorporated areas of the county for the county tax and in the corporate limits of the city for the city tax at a rate not exceeding one-half of one percent of the selling price.

(4) Taxes imposed under this section shall be collected from persons who are taxable by the state under chapter 82.45 RCW upon the occurrence of any taxable event within the unincorporated areas of the county or within the corporate limits of the city, as the case may be.

(5) Taxes imposed under this section shall comply with all applicable rules, regulations, laws, and court decisions regarding real estate excise taxes as imposed by the state under chapter 82.45 RCW.

(6) As used in this section, "city" means any city or town and "capital project" means those public works projects of a local government for planning, acquisition, construction, reconstruction, repair, replacement, rehabilitation, or improvement of streets; roads; highways; sidewalks; street and road lighting systems; traffic signals; bridges; domestic water systems; storm and sanitary sewer systems; parks; recreational facilities; law enforcement facilities; fire protection facilities; trails; libraries; administrative and/or judicial facilities; river and/or waterway flood control projects by those jurisdictions that, prior to June 11, 1992, have expended funds derived from the tax authorized by this section for such purposes; and, until December 31, 1995, housing projects for those jurisdictions that, prior to June 11, 1992, have expended or committed to expend funds derived from the tax authorized by this section or the tax authorized by RCW 82.46.035 for such purposes.

RCW 67.28.1815, Revenue – Special fund – Uses for tourism promotion and tourism facility acquisition and operation, states:

Except as provided in RCW 67.28.180, all revenue from taxes imposed under this chapter shall be credited to a special fund in the treasury of the municipality imposing such tax and used solely for the purpose of paying all or any part of the cost of tourism promotion, acquisition of tourism-related facilities, or operation of tourism-related facilities. Municipalities may, under chapter 39.34 RCW, agree to the utilization of revenue from taxes imposed under this chapter for the purposes of funding a multijurisdictional tourism-related facility.

RCW 84.34.240(1), Acquisition of open space, etc., land or rights to future development by certain entities – Conservation futures fund – Additional requirements, authority, states in part:

(1) Any board of county commissioners may establish by resolution a special fund which may be termed a conservation futures fund to which it may credit all taxes levied pursuant to RCW 84.34.230. Amounts placed in this fund may be used for the purpose of acquiring rights and interests in real property pursuant to the terms of RCW 84.34.210 and 84.34.220, and for the maintenance and operation of any property acquired with these funds. The amount of revenue used for maintenance and operations of parks and recreational land may not exceed fifteen percent of the total amount collected from the tax levied under RCW 84.34.230 in the preceding calendar year. Revenues from this tax may not be used to supplant existing maintenance and operation funding. Any rights or interests in real property acquired under this section must be located within the assessing county. Further, the county must determine if the rights or interests in real property acquired with these funds would reduce the capacity of land suitable for development necessary to accommodate the allocated housing and employment growth, as adopted in the countywide planning policies. When actions are taken that reduce capacity to accommodate planned growth, the jurisdiction shall adopt reasonable measures to increase the capacity lost by such actions.

RCW 36.33A.060, Accumulated moneys, states:

Moneys accumulated in the equipment rental and revolving fund shall be retained therein from year to year; shall be used only for the purposes stated in this chapter; and shall be subject to the budgetary regulations in chapter 36.40 RCW.

RCW Sales and use tax for emergency communication systems and facilities.

(1) A county legislative authority may submit an authorizing proposition to the county voters, and if the proposition is approved by a majority of persons voting, fix and impose a sales and use tax in accordance with the terms of this chapter for the purposes designated in subsection (3) of this section.

(2) The tax authorized in this section shall be in addition to any other taxes authorized by law and shall be collected from those persons who are taxable by the state under chapters 82.08 and 82.12 RCW upon the occurrence of any taxable event within the county. The rate of tax shall equal one-tenth of one percent of the selling price in the case of sales tax, or value of the article used, in the case of a use tax.

(3) Moneys received from any tax imposed under this section shall be used solely for the purpose of providing funds for costs associated with financing, design, acquisition, construction, equipping, operating, maintaining, remodeling, repairing, reequipping, and improvement of emergency communication systems and facilities.

(4) Counties are authorized to develop joint ventures to collocate emergency communication systems and facilities.

(5) Prior to submitting the tax authorization in subsection (2) of this section to the voters in a county that provides emergency communication services to a governmental agency pursuant to a contract, the parties to the contract shall review and negotiate or affirm the terms of the contract.

(6) Prior to submitting the tax authorized in subsection (2) of this section to the voters, a county with a population of more than five hundred thousand in which any city over fifty thousand operates emergency communication systems and facilities shall enter into an interlocal agreement with the city to determine distribution of the revenue provided in this section.