King County Water Quality Enterprise

Financial Statements and
Supplemental Schedule for the Years Ended
December 31, 2003 and 2002 and
Independent Auditors' Report

KING COUNTY WATER QUALITY ENTERPRISE

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INDEPENDENT AUDITORS' REPORT

King County Council
Seattle, Washington

We have audited the accompanying statements of net assets of King County Water Quality Enterprise (the "Enterprise") as of December 31, 2003 and 2002, and the related statements of revenues, expenses and changes in net assets and of cash flows for the years then ended. These financial statements are the responsibility of the Enterprise's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Enterprise as of December 31, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying management's discussion and analysis on pages 2 through 6 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying supplemental schedule of net revenues available for debt service for the year ended December 31, 2003 is presented as required by bond resolutions and is not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied in our audits of the basic financial statements and, in our opinion, is fairly stated in all material respects when considered in relation to the basic financial statements taken as a whole.

Deloitte & Touche LLP

June 14, 2004

KING COUNTY WATER QUALITY ENTERPRISE

MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2003

The management of the King County Water Quality Enterprise ("Water Quality" or the "Enterprise") offers readers of its financial statements this narrative overview and analysis of the financial activities for the fiscal year ended December 31, 2003. It is intended to be viewed in conjunction with the financial statements, which follow this section.

FINANCIAL HIGHLIGHTS

During 2003, Water Quality made significant investments in its continued implementation of the Regional Wastewater Services Plan ("RWSP"). The RWSP is intended to build the extra capacity King County requires to meet future population growth. In 2003, the Enterprise completed the comprehensive process to find a site for the new Brightwater Treatment Plant near Woodinville in Snohomish County, acquired land for Brightwater, and continued to improve conveyance and combined sewer overflow capacity.

Operations of the Enterprise were stable during 2003, with monthly sewer rates unchanged from 2002 at $23.40. 2003 is the second year of a planned three-year level rate for monthly sewer charges. Capacity charge revenues rose $1.9 million reflecting a higher rate of $17.60, a 40-cent increase over 2002. The Enterprise emphasized expense management in 2003 as nondepreciation operating expense rose to $82.9 million, $1.6 million less than the Enterprise's adopted budget. Debt from state loans increased during 2003 as new, low-rate loans were received from the State of Washington to fund the Enterprise's capital program. Low yields and reduced cash balances resulted in a substantial decline in investment earnings.

The results of operations for 2003 produced a debt service coverage ratio on the Enterprise's senior lien debt of 1.46, in excess of the coverage covenant requirement of 1.15 and the King County Council policy objective of 1.25.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Enterprise's basic financial statements. The basic financial statements comprise the financial statements and the notes to the financial statements, which explain certain elements of the financial statements in greater detail.

REQUIRED FINANCIAL STATEMENTS

The Enterprise's financial statements provide information with respect to all of its activities and use accounting methods similar to those used by private-sector companies. The statements provide both long-term and short-term information about the Enterprise's financial status.

The comparative statements of net assets present information on all of the Enterprise's assets and liabilities, with the difference between assets and liabilities presented as net assets as of each year-end. The statements of net assets provide information about the nature and amount of investments in resources (assets) and obligations to creditors (liabilities).

The two most recent years' operating and nonoperating revenues and expenses of the Enterprise are accounted for in the statements of revenues, expenses and changes in net assets. The statements illustrate the current and prior period results of operations and recovery of costs by receipt of fees and are instrumental in demonstrating continued creditworthiness. All changes in net assets are reported as soon as the underlying event occurs, irrespective of the timing of related cash flows. Readers should note that the principal support for Water Quality's activities (about 89.6% of operating revenues in 2003) is receipt of monthly sewage disposal charges from 35 municipal and three nonmunicipal participants in King and Snohomish counties. The receipt of the monthly payments is governed by service agreements, the earliest of which expires in July 2036.

The statements of cash flows report cash receipts, cash payments and net changes in cash derived from operations, financing and investment activities. From the statements, the reader can discern the Enterprise's sources and applications of cash during 2003, reasons for differences between operating cash flows and operating income, and the effect on the statements of net assets from investing, capital and financing activities.

The notes to financial statements provide additional information essential to obtain a full understanding of the data provided in the basic statements.

FINANCIAL ANALYSIS OF THE STATEMENTS OF NET ASSETS

Comparative data, stated in millions of dollars:

	2003	2002	Difference	Percentage Change
Capital assets	$ 1,782.9	$ 1,632.0	$ 150.9	9.2 %
Total assets	2,000.5	1,904.1	96.4	5.1 %
Total liabilities	1,662.8	1,566.8	96.0	6.1 %
Net assets invested in capital assets	228.5	204.8	23.7	11.6 %
Net assets—restricted	78.4	74.1	4.3	5.8 %
Net assets—unrestricted	30.8	58.3	(27.5)	(47.2)%
Net assets	337.7	337.3	0.4	0.1 %

Net assets serve as a useful indicator of the Enterprise's financial position. As of December 31, 2003, assets of the Enterprise exceeded liabilities by $337.7 million.

Of the total assets of the Enterprise, at year-end 2003, 89.1% is invested in capital assets such as treatment plants, pumping and regulator stations, interceptors and other equipment. The Enterprise uses its capital assets to provide wholesale wastewater collection and treatment services in King and Snohomish counties. Current operating and debt service requirements are met by operating and nonoperating revenues composed of monthly sewage disposal charges, a capacity charge for new customers, other special-handling charges, miscellaneous operating revenues and investment earnings.

Net assets increased $439 thousand in 2003 compared to a decrease of $1.0 million in 2002. This relative stability in change of net assets was attributable to stable operating results and offsetting changes in other operating factors.

The Enterprise reports its investment in capital assets, net of debt related to capital asset acquisition, as $228.5 million, an increase of $ 23.7 million (11.6%) over 2002, as investments in capital assets exceeded net new indebtedness. Resources of the Enterprise may be restricted for use in construction, to meet debt service requirements, to satisfy bond covenants, or to meet regulatory restrictions. Restricted net assets at year-end 2003 increased $4.3 million (5.8%), as restricted cash balances increased while liabilities payable from restricted assets decreased. Unrestricted net assets decreased by $27.5 million (47.2%) as transfers to the construction fund reduced operating cash.

FINANCIAL ANALYSIS OF THE STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Comparative data, stated in millions of dollars:

	2003	2002	Difference	Percentage Change
Operating revenues	$ 214.2	$ 213.2	$ 1.0	0.5 %
Operating expenses	170.6	168.0	2.6	1.5 %
Operating income	43.5	45.2	(1.7)	(3.8)%
Nonoperating revenues (expenses)	(52.1)	(59.3)	7.2	(12.1)%
Grant revenues	11.4	13.9	(2.5)	(18.0)%
Change in net assets	0.4	(1.0)	1.4	140.0 %

While the statements of net assets show changes in assets, liabilities, and net assets, the statements of revenues, expenses and changes in net assets provide insight into the source of these changes. During 2003, the statements report that operating revenues increased by $1.0 million (0.5%) and operating expenses increased by $2.6 million (1.5%). These changes were influenced by several factors:

- The Enterprise collected a monthly sewage disposal charge of $23.40 (per month, per residential customer equivalent) in 2003, which is unchanged from 2002. Total sewage disposal fees decreased by $204 thousand (0.1%) in 2003 from 2002 as an increase in residential customers was offset by a decrease in nonresidential usage.

- Other operating revenues, including capacity charge for new customers and other treatment charges, rose $1.1 million (5.4%), reflecting the addition of new connections and an increase in the per month capacity charge from $17.20 in 2002 to $17.60 in 2003 (2.3%) and increases in other charges.

- Nondepreciation-related operating expenses increased $3.2 million (4.1%). Payments to other County agencies, principally for Surface Water Management, increased $3.3 million (13.4%).

The decrease in nonoperating revenues and expenses (net expenses) of $7.3 million (12.3%) was primarily affected by:

- A decline in market yields on short-term investments, combined with the effect of declining Enterprise cash balances during 2003 caused investment earnings to decrease by $5.5 million (74.0%) from 2002.

- Reported interest expense and debt-related amortization decreased $10.8 million as interest incurred on newly issued debt was offset by savings from bond refunding and low short-term and subsidized borrowing rates. Capitalized interest increased $4.7 million as the Enterprise continued its significant capital improvements program.

The statements also report comparative amounts of capital grant revenues for 2003 and 2002:

- Capital grant revenues derived from federal and state agencies decreased $2.5 million in 2003 as reduced federal funding was received for the Enterprise's Denny Way and Renton projects, which are approaching completion of grant-funded portions.

CAPITAL ASSETS

At December 31, 2003, the Enterprise's investment in capital assets, net of accumulated depreciation, is $1.8 billion. This is an increase of $150.9 million (9.2%) over the year-end 2002 investment in capital assets, net of accumulated depreciation. The change is a result of replacement and additions to the interceptor and siphon systems, purchases of land, additional storage capacity, extensions of sewer trunk lines and continued efforts to control odor and improve sewage-handling technology.

The increase of $148.8 million (48.7%) in work in progress is directly related to continued implementation of the Enterprise's Regional Wastewater Services Plan. Capital expenditures in work in progress relate to continued system-wide improvement and expansion. Large 2003 construction project expenditures include:

- $19.1 million added to the Denny Way Combined Sewer Overflow project, a joint venture with Seattle Public Utilities, also partially funded by federal grants

- $16.4 million in 2003 conveyance system improvements

- $35.9 million for the Henderson/Martin Luther King Way Combined Sewer Overflow project

- $10.6 million expended on the North Creek storage facility

- $61.3 million spent toward completion of the Brightwater treatment plant

DEBT ADMINISTRATION

During 2003, the Enterprise benefited from declining interest rates. Rates paid on commercial paper and variable rate debt were substantially below amounts projected in setting the 2003 sewer rate. In April 2003, proceeds from issuance of Sewer Revenue Refunding Bonds, Series 2003A, were used for advance refunding of existing debt. Although a loss was recognized on defeasance, the transaction will reduce aggregate debt service payments by $10.2 million over the life of the bonds. The present value of the reduction of aggregate Enterprise debt service was $5.3 million.

In March 2004, the Enterprise advance refunded a 1999 issue of revenue bonds with issuance of Sewer Revenue Refunding Bonds, Series 2004B. The refunding activity resulted in a reduction of future aggregate debt service of $7.2 million, the present value of which is $4.1 million. In March 2004, the Enterprise also issued Sewer Revenue Bonds, Series 2004A, proceeds of which were used to repay construction-related short-term debt and to fund construction activities of the Enterprise.

During 2003 the Enterprise received new loans from agencies of the State of Washington totaling $49.5 million. The loans carry below-market rates of from 0.5% to 1.5% and repayment terms up to 22 years.

After issuance of the 2003 refunding bonds (which refunded a portion of general obligation debt with revenue bonds), the Enterprise has $363.0 million of general obligation bonds outstanding. Although repaid from a portion of receipts from sewage disposal fees and other income, the full faith and credit of King County guarantees repayment of principal and interest on general obligation bonds.

The Enterprise has $1.0 billion of sewer revenue bonds outstanding. Revenue bonds are repaid from and secured by a pledge of earnings, revenues and money received by the Enterprise and King County from or on account of operation of the sewer system, to include receipts from sewage disposal fees and other income of the Enterprise. Revenue bonds are not guaranteed by the full faith and credit of King County.

At time of the issuance of the Sewer Revenue Refunding Bonds, Series 2003A, the Enterprise's bond ratings, as conditioned upon the delivery of an accompanying municipal bond insurance policy, are:

Moody's Investor Services	Standard & Poor's
Aaa	AAA

Underlying ratings (those assigned by the ratings services without benefit of an accompanying municipal bond insurance policy) are "A1" for Moody's Investor Services and "AA-" for Standard & Poor's.

As required by bond covenant, the Enterprise maintains a bond reserve account, which is funded by cash balances and surety policies. At December 31, 2003, the cash balance in the reserve account was $67.2 million. In addition to bond covenant reserves, the Enterprise also maintains financial policy reserves. At December 31, 2003, the liquidity and asset management financial policy reserves totaled $18 million.

REQUESTS FOR INFORMATION

This financial report is designed to provide an overview of the Enterprise's financial condition at December 31, 2003, and results for the period then ended. Questions concerning this report or requests for additional information should be addressed to Connie L. Griffith, Chief Accountant for King County, 500 Fourth Avenue, Room 653, Seattle, Washington 98104.

KING COUNTY WATER QUALITY ENTERPRISE

STATEMENTS OF NET ASSETS
DECEMBER 31, 2003 AND 2002

ASSETS	2003	2002
CURRENT ASSETS:		
Cash and cash equivalents	$ 10,055,566	$ 30,453,117
Accounts receivable	13,885,039	12,974,824
Inventory of supplies	4,319,347	4,232,433
	28,259,952	47,660,374
NONCURRENT ASSETS:		
Revenue fund:		
Cash and cash equivalents	21,829,755	29,826,841
Construction fund:		
Cash and cash equivalents	9,076,990	54,492,722
Grants receivable	1,800,466	1,413,943
Accounts receivable	4,288,082	730,429
Due from other funds	278,644	
Due from other governments	52,198	190,741
Bond fund:		
Cash and cash equivalents	136,402,049	122,541,239
	173,728,184	209,195,915
CAPITAL ASSETS:		
Building and land improvements	1,276,927,890	1,215,002,799
Plant in service and other equipment	864,316,230	852,374,477
Less accumulated depreciation	(862,711,327)	(776,059,971)
	1,278,532,793	1,291,317,305
Land	50,073,118	35,185,252
Construction work in progress	454,297,338	305,523,698
	1,782,903,249	1,632,026,255
OTHER:		
Deferred environmental remediation costs	6,811,322	7,048,694
Other deferred charges	8,807,142	8,138,266
	15,618,464	15,186,960
TOTAL	$ 2,000,509,849	$ 1,904,069,504

(Continued)

KING COUNTY WATER QUALITY ENTERPRISE

STATEMENTS OF NET ASSETS
DECEMBER 31, 2003 AND 2002

LIABILITIES AND NET ASSETS	2003	2002
CURRENT LIABILITIES:		
Accounts payable	$ 2,532,580	$ 9,751,466
Interest payable	550,057	279,906
Wages and benefits payable	9,883,170	10,553,560
Notes payable	100,000,000	93,300,000
Obligations under reverse repurchase agreements	434,035	458,504
State loans payable	2,079,187	1,340,484
Due to other funds	2,219,513	1,384,438
Estimated claims settlement	2,103,607	865,894
	119,802,149	117,934,252
CURRENT LIABILITIES PAYABLE FROM RESTRICTED ASSETS:		
Loan from King County Pool	44,967,935	
Accounts payable	28,847,427	20,146,539
Interest payable	33,691,551	29,216,396
Wages and benefits payable	256,728	700,870
Due to other funds		1,720,049
Obligations under reverse repurchase agreements	5,510,284	3,333,872
General obligation bonds payable—current portion	6,950,000	6,605,000
Revenue bonds payable—current portion	20,700,000	10,835,000
Estimated claims settlement	6,662,042	6,662,042
	147,585,967	79,219,768
NONCURRENT LIABILITIES:		
General obligation bonds payable	356,060,000	450,470,000
Revenue bonds payable	1,017,355,000	941,585,000
Deferred bond premium, discount, and refunding losses	(62,324,720)	(59,275,841)
State loans payable	84,311,900	36,855,347
	1,395,402,180	1,369,634,506
Total liabilities	1,662,790,296	1,566,788,526
NET ASSETS:		
Invested in capital assets—net of related debt	228,500,258	204,792,287
Restricted	78,383,158	74,145,082
Unrestricted	30,836,137	58,343,609
Total net assets	337,719,553	337,280,978
TOTAL	$ 2,000,509,849	$1,904,069,504

See notes to financial statements. (Concluded)

KING COUNTY WATER QUALITY ENTERPRISE

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2003 AND 2002

	2003	2002
OPERATING REVENUES:		
Sewage disposal fees	$ 191,919,371	$ 192,123,662
Other operating revenues	22,238,333	21,099,526
	214,157,704	213,223,188
OPERATING EXPENSES:		
Sewage treatment, disposal and transmission	71,704,414	70,024,576
General and administrative	11,182,789	9,615,021
Depreciation and amortization	87,722,739	88,381,507
	170,609,942	168,021,104
OPERATING INCOME	43,547,762	45,202,084
NONOPERATING REVENUES (EXPENSES):		
Investment earnings	1,918,279	7,385,863
Interest	(52,712,603)	(53,088,532)
Amortization of bond premium, discount and issuance costs	(5,275,865)	(15,747,927)
Loss on disposal of fixed assets and environmental remediation	(686,278)	(1,188,358)
Other	4,702,364	3,291,533
	(52,054,103)	(59,347,421)
LOSS BEFORE GRANTS, CONTRIBUTIONS, AND TRANSERS	(8,506,341)	(14,145,337)
GRANT REVENUES	11,438,426	13,914,612
CAPITAL CONTRIBUTIONS	544,470	
TRANSFERS—Net	(3,037,980)	(764,865)
CHANGE IN NET ASSETS	438,575	(995,590)
NET ASSETS:		
Beginning of year	337,280,978	338,276,568
End of year	$ 337,719,553	$ 337,280,978

See notes to financial statements.

KING COUNTY WATER QUALITY ENTERPRISE

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2003 AND 2002

	2003	2002
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from customers	$ 209,828,378	$ 213,649,253
Cash payments to suppliers for goods and services	(51,841,197)	(41,086,196)
Cash payments for employee services	(31,929,069)	(31,932,216)
Net cash provided by operating activities	126,058,112	140,630,841
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:		
Operating transfers out	(2,493,510)	(764,865)
Interest paid on short-term loans	(748,503)	(14,266)
Net cash used in noncapital financing activities	(3,242,013)	(779,131)
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Acquisition of capital assets	(170,942,771)	(156,601,534)
Principal paid on general obligation bonds	(6,605,000)	(8,635,000)
Interest paid on general obligation bonds	(21,428,391)	(24,488,919)
Proceeds of new bond issuance	96,470,000	446,130,000
Principal paid on bonds by refunding	(87,460,000)	(360,490,000)
Principal paid on revenue bonds	(10,835,000)	(23,775,000)
Interest paid on revenue bonds	(41,191,747)	(37,627,682)
Principal paid on notes payable	6,700,000	9,800,000
Interest paid on notes payable	(1,197,481)	(1,501,236)
Issuance costs of bonds and notes payable	(8,993,616)	461,726
Principal paid on state loans	(1,341,273)	(45,035,544)
Proceeds of state loans	49,536,529	24,457,000
Interest paid on state loans	(432,396)	(1,308,274)
Capital grants received	11,051,902	14,289,307
Environmental remediation and amortization of deferred charges	(166,636)	(604,462)
Net cash used in capital and related financing activities	(186,835,880)	(164,929,618)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investment securities		(15,393,057,500)
Proceeds from sales of investment securities		15,428,073,777
Interest, other gains on investments and changes in reverse repurchase obligations	4,070,222	10,670,939
Net cash provided by investing activities	4,070,222	45,687,216

(Continued)

KING COUNTY WATER QUALITY ENTERPRISE

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2003 AND 2002

	2003	2002
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	$ (59,949,559)	$ 20,609,308
CASH AND CASH EQUIVALENTS:		
Beginning of year	237,313,919	216,704,611
End of year	$ 177,364,360	$ 237,313,919
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Operating income	$ 43,547,762	$ 45,202,084
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	87,722,739	88,381,507
Changes in assets:		
Accounts receivable	(4,467,869)	(1,273,931)
Inventory of supplies	(86,914)	(66,419)
Due from other governments	138,544	1,699,996
Changes in liabilities:		
Accounts payable	1,482,001	8,826,807
Wages and benefits payable	(1,114,533)	1,015,315
Due to other funds	(1,163,618)	(3,154,518)
Total adjustments	82,510,350	95,428,757
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 126,058,112	$ 140,630,841
SUPPLEMENTAL DISCLOSURES OF NONCASH CAPITAL AND RELATED FINANCING ACTIVITIES—Contribution of capital assets from government	$ 544,470	$
NONCASH INVESTING ACTIVITIES—Changes in fair value of investments	$ (1,001,813)	$ 2,510,372

See notes to financial statements. (Concluded)

1. OPERATIONS AND ACCOUNTING POLICIES

Summary of Operations—The King County Water Quality Enterprise (the "Enterprise") is an enterprise fund operated by the King County Department of Natural Resources in accordance with Chapter 35.58 of the Revised Code of Washington ("RCW") to provide water pollution abatement services to the urbanized areas of King County, Washington (the "County").

The Enterprise is an integral part of the County reporting entity and is included, as an enterprise fund, in the County's comprehensive annual financial report.

As an enterprise fund, the Enterprise is funded and operated separately from other operations of the County. Revenues, bond proceeds and grants-in-aid are restricted by purpose. Accordingly, the Enterprise has separate accounting records and financial statements.

The Enterprise has long-term sewage disposal agreements with the cities and sewer districts that operate sewage collection systems within its service area. The monthly sewage disposal charge to the contracting cities and districts is based on the Enterprise's estimated annual monetary requirements, including operating costs and debt service. Revenues from the Enterprise's largest customer, the City of Seattle (Seattle Public Utilities), represent approximately 43.5% and 45.5% of total sewage disposal fees in 2003 and 2002, respectively.

The Enterprise purchases goods and services from other County agencies, including reimbursement of the County's General Fund for a share of general government. Expenses incurred in doing business with other County agencies amounted to $28,327,000 and $24,978,000 in 2003 and 2002, respectively.

Significant Accounting Policies—The Enterprise is accounted for on a flow of economic resources measurement focus similar to that of a private enterprise organized for profit. The Enterprise's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to governmental units using the accrual basis of accounting. Under this method, revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred. The Enterprise, in accordance with Governmental Accounting Standards Board ("GASB") Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, elected not to apply all statements of the Financial Accounting Standards Board issued subsequent to November 30, 1989.

a. *Cash and Cash Equivalents*—The Enterprise considers as cash and cash equivalents all balances held with the King County Treasurer in the King County Investment Pool (the "Pool") and petty cash. Unrealized gain or loss on the Enterprise's proportionate share of the Pool is reported as a component of investment earnings.

b. *Due to/from Other County Funds*—Due to/from other funds consists of payments for goods and services or advances provided to or by other funds and for cash collected on behalf of or due from another fund.

c. *Inventory of Supplies*—Inventory is recorded at the lower of cost or market using the weighted-average cost method. Inventory is written off in the year that it is determined obsolete.

d. *Restricted Assets*—In accordance with the Enterprise's bond resolutions, state law, or other agreements, separate restricted assets have been established. These assets are restricted for specific purposes, including debt service payments and funding of capital projects. These funds are maintained in the revenue fund, construction fund and bond fund on the statements of net assets.

e. *Capital Assets*—The provision for depreciation is made on a straight-line basis over the estimated useful lives of the Enterprise's capital assets, which range from two to 50 years.

Total interest incurred was $69,743,823 and $65,414,868 during the years ended December 31, 2003 and 2002, respectively, of which $17,031,220 and $12,326,336 was capitalized.

Repairs and maintenance are expensed as incurred; major renewals, replacements and betterments are capitalized.

The Enterprise periodically reviews long-lived assets for impairment to determine whether any events or circumstances indicate the carrying value of the assets may not be recoverable. No impairment was identified in 2002 or 2003.

f. *Environmental and Property Remediation Costs*—In prior years, the Enterprise settled lawsuits related to certain environmentally damaged sites. In these settlements, the Enterprise agreed to pay its portion of remediation and cleanup costs.

The Enterprise funds the majority of its environmental expenditures with debt proceeds. The Enterprise also receives grant funding to offset a portion of these costs. The initial settlement costs, net of the partial grant funding and other recoveries, are deferred and are being amortized over 40 years as revenues are collected from the Enterprise's customers. Current remediation activities are expensed in the year incurred. Previously, the Enterprise agreed to pay a portion of remediation costs to clean up contaminated sediments and restore aquatic habitats in Elliott Bay and the Lower Duwamish River. During 2003, the Enterprise incurred net costs of $166,636 with respect to Elliott Bay and the Lower Duwamish River.

g. *Compensated Absences*—Employees earn vacation based upon their date of hire and years of service. They may accumulate a maximum of 480 hours. Unused vacation at retirement or normal termination is considered vested and payable to the employee.

Employees also earn up to 12 days of sick leave per year and may accumulate sick leave balances without limit. Employees or their beneficiaries are paid 35% of the accrued unused sick leave upon retirement or death. No amounts are paid for unused sick leave upon termination.

The Enterprise records additions to wages and benefits payable for accrued and unused vacation and sick leave in the period earned.

h. *Amortization*—Bond issue costs and discounts are amortized to interest expense using the effective interest rate method over the term of the bonds.

The excess costs incurred over the carrying value of bonds refunded on early extinguishment of debt are amortized as a component of interest expense over the shorter of the remaining term of the refunded bond or the term of the new bond.

i. *Deferred Compensation*—The County offers a consolidated deferred compensation plan that complies with Internal Revenue Code Section 457. The plan permits employees to defer a portion of annual compensation until future years. Participation in the plan is voluntary. No amounts related to these obligations are recorded in the financial statements.

j. *Use of Estimates*—The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Changes in these estimates and assumptions are considered reasonably possible and may have a material impact on the financial statements.

k. *Reclassifications*—Certain reclassifications have been made to the prior year statements to conform to the current year presentation.

l. *Capital Grant Revenues*—Pursuant to GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, grant revenues are included in nonoperating revenues as capital grant revenues. The Enterprise received capital grant revenues of $11,438,426 and $13,914,612 for the years ended December 31, 2003 and 2002, respectively.

m. *Net Assets*—Pursuant to GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, grant revenues and resources set aside for repayment of bonds, net of related liabilities are classified as restricted net assets on the statement of net assets, as their use is limited by externally-imposed restrictions. Capital assets are reported as a separate component of net assets, net of related debt. Any net assets not subject to classification as restricted or invested in capital assets are reported as unrestricted.

New Accounting Standards Adopted—In 2002, the Enterprise adopted GASB Statements No. 34, No. 37, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments: Omnibus—an amendment of GASB Statements No. 21 and No. 34*, and No. 38, *Certain Financial Statement Note Disclosures*.

In addition to other presentation changes, GASB Statement No. 34 (as amended by GASB Statement No. 37) requires that amounts reported as contributed capital and retained earnings in prior years be reported as net assets within a statement of net assets. GASB Statement No. 34 also requires that the basic financial statements be preceded by a Management's Discussion and Analysis, which is required supplementary information. Pursuant to GASB Statement No. 38, certain note disclosures have been added or amended.

In March 2003, the GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures*. This statement establishes and modifies disclosure requirements related to investment risks: credit risk (including custodial credit risk and concentrations of credit risk), interest rate risk and foreign currency risk. This statement also establishes and modifies disclosure requirements for deposit risks: custodial credit risk and foreign currency risk. The requirements of this statement are effective for the Enterprise's financial statements for periods beginning after June 15, 2004 (January 1, 2005). The Enterprise is in the process of determining the impact of this standard on its financial statements.

GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, establishes accounting and financial reporting standards for impairment of capital assets. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. This statement also clarifies and establishes accounting requirements for insurance recoveries. The Enterprise will adopt this statement effective January 1, 2005; however, the Enterprise does not expect a material impact on its financial position or results of operations.

In June 2003, the GASB issued Technical Bulletin No. 2003-1 ("TB 03-1"), *Disclosure Requirements for Derivates Not Reported at Fair Value on the Statement of Net Assets*, which supersedes Technical Bulletin 94-1 and clarifies guidance on derivative disclosures, pending the results of the GASB's project on reporting and measurement of derivatives and hedging activities. TB 03-1 is effective for fiscal years ending after June 15, 2003, and was adopted by the Enterprise in 2003 without material impact to financial position or operation.

2. CASH AND INVESTMENTS

The King County Treasurer is the custodian of the Enterprise's cash and investments. Prior to October 2002, most Enterprise funds were invested solely in direct obligations of the U.S. Treasury. A refunding of bonds, which were issued with various restrictive covenants, has removed this investment restriction and enabled the Enterprise to invest all its funds in the Pool. Enterprise cash on deposit with the King County Treasurer is pooled with cash from other County funds and other jurisdictions and either deposited in the County's bank account or invested by the County. The County's pooled deposits and investments are categorized by risk into three basic categories. Risk Category 1 includes deposits insured or collateralized with securities held by the entity or by its agent in the entity's name. Risk Category 2 includes deposits collateralized with securities held by the pledging financial institution's trust department or agent in the entity's name. Risk Category 3 includes deposits that are uncollateralized, including any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent, but not in the entity's name. At year-end 2003, all of the County's pooled deposits are in Risk Category 1.

Statutes permit the Pool to enter into reverse repurchase agreements. The Enterprise has been allocated a proportionate share of the pooled investments and liabilities associated with reverse repurchase agreements based on total equity in the Pool. Reverse repurchase agreements are recorded as an increase to assets and an offsetting increase to liabilities. The Enterprise's share of the reverse repurchase agreements was $5,944,319 and $3,792,376 as of December 31, 2003 and 2002, respectively. The proceeds from the repurchase agreements are reinvested in other instruments with the same maturity as the collateral securities, resulting in a matched position.

The amount of cash received in reverse repurchase agreements is normally less than the market value of the underlying security. Should a third party default on their obligations to resell these securities to the County, the County would be faced with an economic loss equal to the difference between the market value of the underlying securities and the agreement obligation. During the fiscal years ended December 31, 2003 and 2002, no losses were incurred as a result of default.

3. RISK MANAGEMENT

The Enterprise is exposed to a wide range of risks of loss, including those related to tort; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

The Enterprise participates in three County internal service funds to account for and finance property/casualty, workers' compensation and employee medical and dental benefits self-insurance programs. The County contracts with a plan administrator to process medical and dental claims. County fund/claims managers, together with the Civil Division of the King County Prosecuting Attorney's Office, are responsible for processing all tort and workers' compensation claims.

Claims settlements and loss expenses are accrued in the three internal service funds for the estimated settlement value of both reported and unreported claims. These funds are responsible for collecting inter-fund premiums from insured funds and departments, for paying claim settlements, and for purchasing certain policies. The County's internal service funds assess premiums attributable to the Enterprise on the basis of claims experience, actuarial evaluation of future claims risk, and adequacy of available reserves. Premiums are recorded as an expense in the year paid or accrued.

The Enterprise retains all risk associated with environmental claims.

4. LONG-TERM LIABILITIES AND NOTES PAYABLE

Sewer Revenue Bonds—As of December 31, 2003, bonds outstanding include $528,855,000 of serial bonds maturing from January 1, 2004 through 2028, bearing interest at stated rates of 2% to 6.25% per annum, and $509,200,000 of term bonds maturing on January 1 in the years 2018 through 2035, bearing interest at stated rates of 5% to 6.2% per annum.

In April 2003, the Enterprise issued $96,470,000 of sewer revenue bonds maturing from January 1, 2004 to 2035. The issue includes $56,460,000 of serial bonds maturing from January 1, 2004 through 2028, bearing interest at stated rates of 2% to 5.5%, and $40,010,000 of term bonds, maturing January 1, 2029 to 2035, bearing interest at a stated rate of 5%.

Certain serial bonds may not be redeemed prior to maturity; other bonds may be redeemed at declining premiums after the lapse of specific periods of time. Monies in the sewer revenue bond fund may be used to purchase term bonds prior to maturity.

Payments from revenues of the Enterprise are required to be made to the sewer revenue bond fund in annual amounts sufficient to retire serial or term bonds on or before maturity. At December 31, 2003, the Enterprise designated restricted cash balances of $45,072,704 as amounts to repay principal and interest due on revenue bonds on January 1, 2004.

Pursuant to bond resolutions and covenants, additional amounts of $67,182,625, held in the bond fund as bond reserves, as of both December 31, 2003 and 2002 have been designated as net assets restricted for future debt service. The Enterprise met additional reserve requirements required by the issuance of Sewer Revenue Refunding Bonds, Series 2003A, by purchase of a surety policy issued by a private insurer.

Defeased Debt—In April 2003, the Enterprise issued $96,470,000 of Sewer Revenue Refunding Bonds, Series 2003A. Bond proceeds were used for advance refunding of existing general obligation debt and to pay costs of issuance, bond insurance and underwriter's discount. The loss recognized on defeasance was $10,217,787, which will be amortized over the life of the old bonds. The transaction will reduce aggregate debt service payments by $10,241,386 over the life of the bonds. The present value of the reduction of aggregate debt service is $5,309,450.

The following outstanding bonds were considered defeased as of December 31, 2003:

Issue	
Limited Tax General Obligation Bonds, 1994 Series A	$ 151,990,000
Limited Tax General Obligation Bonds, 1995	87,460,000
	$ 239,450,000

At the time of defeasance, amounts are placed in irrevocable escrow accounts to provide for all future debt service on the defeased bonds. As a result, the bonds are considered to be defeased and are not included in the Enterprise's financial statements.

General Obligation Bonds—As of December 31, 2003, bonds outstanding include $102,130,000 of serial bonds maturing January 1, 2004 through 2018, bearing interest at stated rates of 4.75% to 5.8% per annum. General obligation bonds outstanding also include $260,880,000 of term bonds maturing on January 1, 2017 through 2034, bearing interest at stated rates of 4.75% to 6.25% per annum.

Certain serial bonds cannot be redeemed prior to maturity; other bonds may be redeemed at declining premiums after the lapse of specific periods of time.

State Loans—The Enterprise has received loans from the Washington Department of Ecology under the Water Pollution Control State Revolving Fund Loan Program and the Washington Public Works Trust Fund. The loans require annual payments of principal and interest from 2004 through 2026 and bear interest at stated rates from 0.5% and 1.5%. As of December 31, 2003, the balance due on all state loans is $86,391,087. As required by loan covenants, the Enterprise maintains separate cash reserves of $1,646,967 with respect to the loans from the Revolving Fund Loan Program.

Maturities of Long-Term Liabilities—As of December 31, 2003, required principal and interest payments are as follows:

Year(s) Beginning	Revenue Bonds Principal	Revenue Bonds Interest	Revenue Bonds Principal	Revenue Bonds Interest
January 1, 2004	$ 20,700,000	$ 48,593,518		$ 1,400,000
January 1, 2005	19,550,000	47,614,018		1,400,000
January 1, 2006	22,680,000	46,645,668		1,400,000
January 1, 2007	24,435,000	45,531,168		1,400,000
January 1, 2008	25,630,000	44,368,893		1,400,000
January 1, 2009-2013	149,235,000	200,699,949		7,000,000
January 1, 2014-2018	152,995,000	157,215,186		7,000,000
January 1, 2019-2023	110,190,000	124,032,877		7,000,000
January 1, 2024-2028	142,260,000	92,175,637		7,000,000
January 1, 2029-2033	183,190,000	51,486,034	$100,000,000	5,600,000
January 1, 2034-2035	87,190,000	6,748,055		
	$938,055,000	$865,111,003	$100,000,000	$40,600,000

Year(s) Beginning	General Obligation Bonds Principal	General Obligation Bonds Interest	State Loans Principal	State Loans Interest	Total
January 1, 2004	$ 6,950,000	$ 18,598,287	$ 2,079,187	$ 433,804	$ 98,754,796
January 1, 2005	7,970,000	18,225,200	2,107,847	411,299	97,278,364
January 1, 2006	6,215,000	17,821,763	4,352,068	1,107,421	100,221,920
January 1, 2007	6,005,000	17,511,850	4,405,220	1,050,265	100,338,503
January 1, 2008	6,270,000	17,213,638	4,271,672	992,308	100,146,511
January 1, 2009-2013	36,320,000	81,067,139	22,196,503	4,077,395	500,595,986
January 1, 2014-2018	39,970,000	72,188,876	23,657,240	2,524,354	455,550,656
January 1, 2019-2023	60,600,000	60,071,515	20,400,215	932,599	383,227,206
January 1, 2024-2028	76,360,000	43,321,815	2,921,135	32,891	364,071,478
January 1, 2029-2033	107,060,000	20,440,715			467,776,749
January 1, 2034-2035	9,290,000	487,725			103,715,780
	$363,010,000	$366,948,523	$ 86,391,087	$11,562,336	$2,771,677,949

The future annualized interest payments for the variable rate revenue bonds are estimated to be equivalent to the rate of 1.4% incurred during the year ended December 31, 2003.

Changes in Long-Term Liabilities—Long-term liability activity for the years ended December 31, 2003 and 2002 was as follows:

	Revenue Bonds Payable	General Obligation Bonds Payable	State Loans Payable
January 1, 2002	$ 890,555,000	$465,710,000	$ 58,774,376
Additions	446,130,000		24,457,000
Reductions	(384,265,000)	(8,635,000)	(45,035,545)
December 31, 2002	952,420,000	457,075,000	38,195,831
Additions	96,470,000		49,536,529
Reductions	(10,835,000)	(94,065,000)	(1,341,273)
December 31, 2003	$1,038,055,000	$363,010,000	$ 86,391,087
Due within one year	$ 20,700,000	$ 6,950,000	$ 2,079,187

Commercial Paper (Notes Payable)—In December 1995, the Enterprise initiated a commercial paper program that gives the Enterprise the ability to issue up to $100,000,000. The program is supported by an annually renewable line of credit that is scheduled to expire August 11, 2004. It is the intent of the Enterprise to obtain an extension of the line of credit prior to its expiration. As of December 31, 2003, $100,000,000 was issued and outstanding under this program. The commercial paper has maturities ranging between 30 and 154 days and is classified as a current liability of the Enterprise's operating fund.

Variable Rate Revenue Bonds—The variable rate bonds are supported by an annually renewable letter of credit scheduled to expire August 10, 2004. It is the intent of the Enterprise to obtain an extension of the line of credit prior to its expiration.

Financial Policy Reserves—In addition to bond reserves related to Sewer Revenue Bonds, the Enterprise maintains liquidity and asset management reserves in noncurrent assets totaling $18,032,484 at December 31, 2003.

5. CHANGES IN CAPITAL ASSETS

Changes in capital assets for the years ended December 31, 2003 and 2002 are shown in the following tables:

	January 1, 2002	Increases	Retirements and Dispositions	December 31, 2002
Building and land improvements	$1,137,788,974	$ 77,219,825	$ (6,000)	$1,215,002,799
Major equipment and vehicles	7,906,918	320,856	(358,014)	7,869,760
Shop and other equipment	825,452,915	20,061,013	(9,435,434)	836,078,494
Software development	12,690,859		(4,264,636)	8,426,223
Land	33,908,047	1,277,205		35,185,252
Work in progress	226,195,841	158,699,103	(79,371,246)	305,523,698
	2,243,943,554	257,578,002	(93,435,330)	2,408,086,226
Less accumulated depreciation and amortization:				
Building and land improvements	(363,580,078)	(30,399,776)	3,544,419	(390,435,435)
Major equipment and vehicles	(1,790,240)	(686,991)	39,847	(2,437,384)
Shop and other equipment	(316,521,240)	(61,221,463)	2,978,066	(374,764,637)
Software development	(12,630,800)	(56,352)	4,264,637	(8,422,515)
	(694,522,358)	(92,364,582)	10,826,969	(776,059,971)
	$1,549,421,196	$165,213,420	$ (82,608,361)	$1,632,026,255

	January 1, 2003	Increases	Retirements and Dispositions	December 31, 2003
Building and land improvements	$1,215,002,799	$ 61,925,091	$ -	$1,276,927,890
Major equipment and vehicles	7,869,760	310,867	(7,697)	8,172,930
Shop and other equipment	836,078,494	12,341,591	(694,018)	847,726,067
Software development	8,426,223		(8,990)	8,417,233
Land	35,185,252	14,887,866		50,073,118
Work in progress	305,523,698	240,471,599	(91,697,959)	454,297,338
	2,408,086,226	329,937,014	(92,408,664)	2,645,614,576
Less accumulated depreciation and amortization:				
Building and land improvements	(390,435,435)	(29,857,617)		(420,293,052)
Major equipment and vehicles	(2,437,384)	(708,109)	7,898	(3,137,595)
Shop and other equipment	(374,764,637)	(56,715,501)	613,397	(430,866,741)
Software development	(8,422,515)	(412)	8,988	(8,413,939)
	(776,059,971)	(87,281,639)	630,283	(862,711,327)
	$1,632,026,255	$242,655,375	$ (91,778,381)	$1,782,903,249

6. EMPLOYEE BENEFIT PLANS

Defined Benefit Pension Plans—Substantially all full-time and qualifying part-time employees participate in the Public Employees' Retirement System ("PERS"). PERS is a statewide local governmental retirement system administered by the Washington State Department of Retirement Systems, under cost-sharing, multiple-employer defined benefit public employee retirement systems.

Historical trend and other information regarding PERS are presented in the Washington State Department of Retirement Systems' 2003 Comprehensive Annual Financial Report. A copy of this report may be obtained from Department of Retirement Systems, P.O. Box 48380, Olympia, Washington, 98504-8380.

Public Employees Retirement System—The Washington State Legislature (the "Legislature") established PERS in 1947 under RCW chapter 41.40. PERS is a cost-sharing, multiple-employer defined benefit system.

The PERS plan contains three tiers. Participants who joined the system by September 30, 1977 are Plan I members. Those joining thereafter are enrolled in Plan II, unless the employee chooses Plan III. Retirement benefits for all plans are financed from employee and employer contributions and investment earnings. Retirement benefits are vested after various minimum periods of eligible service.

Plan I members are eligible for retirement after 30 years of service or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2% of the final average salary per year of service, capped at 60%. If qualified, after reaching age 66, a limited cost of living allowance is granted.

Plan II members may retire at the age of 65 with five years of service or at 55 with 20 years of service, with an allowance of 2% per year of service of the final average salary. Plan II retirements prior to the age of 65 are actuarially reduced. There is no cap on years-of-service credit and a limited cost-of-living allowance is granted.

Plan III commenced September 1, 2002. Plan III members may retire with 10 years of service or with five service years, including one year earned after age 54 and five service years under Plan II prior to transfer to Plan III. Plan III retirements prior to age 65 are actuarially reduced. With respect to the defined benefit portion of Plan III, there is no cap on years-of-service credit, and a limited cost of living allowance is granted.

Each biennium, the Legislature establishes Plan I employer contribution rates, Plan II employer and employee contribution rates and Plan III employer contribution rates. Employee contribution rates for Plan I are not necessarily adequate to fully fund the system. The employer and employee contribution rates for Plan II and the employer contribution rates for Plan III are developed by the Office of the State Actuary to fully fund future pension obligations. All employers are required to contribute at the level established by the Legislature.

The Enterprise's contribution rates expressed as a percentage of covered payrolls were as follows as of December 31, 2003:

	PERS Plan I 1/1–6/30	**PERS Plan I 7/1–12/31**	**PERS Plan II 1/1–6/30**	**PERS Plan II 7/1–12/31**	**PERS Plan III 1/1-6/30**	**PERS Plan III 7/1-12/31**
Employer	1.32 %	1.40 %	1.32 %	1.40 %	1.32 %	1.40 %
Employee	6.00 %	6.00 %	0.65 %	1.18 %	5%-15%	5%-15%
	7.32 %	7.40 %	1.97 %	2.58 %	6.32%-16.32%	6.40%-16.40%

Employer contributions to Plan III are the same as those required for Plan II. Employee contributions to Plan III are made to a separate defined contribution account and may vary from 5% to 15%.

The Enterprise's required employer contributions for the years ended December 31 were:

	PERS Plan I	PERS Plans II and III
2003	$ 51,165	$ 335,888
2002	82,958	472,152
2001	211,000	1,035,000

7. OPERATING SUBSIDIES AND GRANT REVENUES

Various federal and state government agencies make grants to the Enterprise to aid in financing construction costs (capital grants), including those on various projects included in the comprehensive plan, and for operating costs (operating subsidies). Operating subsidies are recorded as revenues in the statements of revenues, expenses and changes in retained earnings. Capital grants amounted to $11,438,426 and $13,914,612 for the years ended December 31, 2003 and 2002, respectively.

Capital grants and operating subsidies are subject to audit. Expenditures subsequently determined to be disallowed may result in liabilities for the Enterprise to the original granting organization. Management uses its best efforts to determine that grant-funded expenditures are in accordance with grant terms. During 2000, completion of an Environmental Protection Agency ("EPA") audit of the Fort Lawton sewer construction project resulted in a claim against the Enterprise of $6,662,042, representing unsupported and ineligible costs previously paid with grant funds. While the Enterprise has appealed the EPA finding, it recorded the full amount of the claim as a liability at December 31, 2000. As of December 31, 2003, the matter remains unresolved and under appeal.

8. COMMITMENTS AND CONTINGENCIES

Construction Program—The Federal Water Pollution Control Act requires that municipal sewage be subjected to secondary treatment. Major facilities have been included in the Enterprise's construction plan to meet this requirement, including five treatment plants that are being improved or modified to provide secondary treatment under compliance schedules that have been or will be established by permit, by court-approved consent decree, or by administrative order.

The Enterprise is continuing to design, acquire and construct treatment facilities and conveyance lines within the guidelines of the construction plan. As of December 31, 2003, the Enterprise plans to expend approximately $2,036,097,770 through 2009 to complete the requirements of the construction plan. The majority of the expenditures will be used for construction of secondary treatment facilities (including an additional sewage treatment plant) and combined sewer overflow control facilities.

Contingencies and Claims—The Enterprise has received claims from contractors involved in construction projects. The contractors have claimed an amount in excess of the original contract sum. The Enterprise intends to defend its case in these actions and cannot assess the likelihood of an adverse outcome; however, management believes any adverse outcome would not have a material impact on the Enterprise.

Office Facilities—The Enterprise currently rents office space from the Department of Construction and Facilities Maintenance of King County. The Enterprise has not entered into a formalized legal contract for the use of these spaces but is expected to continue to rent office space for future years. Rent expenses incurred in 2003 and 2002 were approximately $1,282,000 and $1,242,000, respectively.

9. TRANSFERS AND CAPITAL CONTRIBUTIONS

The King County Council approves ordinances and/or motions authorizing the Enterprise to contribute and receive amounts to and from various County funds. These net amounts are reported as transfers on the statements of revenues, expenses and changes in net assets. During 2003 and 2002, the net cash transfers to other funds from the Enterprise were $3,037,980 and $764,865, respectively.

During 2003, the Enterprise received capital contributions of capital assets in the amount of $544,470 from an independent authority, which is reported as a component unit of King County.

10. SUBSEQUENT EVENT

In March 2004, the Enterprise issued $185,000,000 of Sewer Revenue Bonds, Series 2004A and $61,760,000 of Sewer Revenue Refunding Bonds, Series 2004B. The proceeds of 2004A were used to repay short-term indebtedness and to fund the Enterprise's ongoing program to improve and maintain the sewer system. The proceeds of 2004B were used for advance refunding of existing revenue bond debt and to pay costs of issuance, bond insurance and underwriter's discount. The loss recognized on defeasance was $8,662,168, which will be amortized over the life of the old bonds. The transaction will reduce aggregate debt service payments by $7,195,082 over the life of the bonds. The present value of the reduction of aggregate debt service is $4,069,301.

* * * * * *

KING COUNTY WATER QUALITY ENTERPRISE

SUPPLEMENTAL SCHEDULE OF NET REVENUES AVAILABLE FOR DEBT SERVICE
YEAR ENDED DECEMBER 31, 2003

The Enterprise is obligated by applicable bond ordinances to set sewage disposal rates at a level adequate to provide net revenue equal to at least 1.15 times the annual debt service requirements for sewer revenue and general obligation bonds payable from revenues of the Enterprise. It is adopted policy of the Enterprise to achieve a debt service coverage ratio of 1.25.

Coverage (1.15 required by covenant, adopted policy 1.25)	1.46

In 2001 the Enterprise adopted a new debt service target of 1.15 times the annual debt service for bonds, obligations, notes and loans of the Enterprise.

Coverage (1.15 adopted target)	1.41

The Enterprise is required to generate revenues sufficient to pay all costs of operation of the sewage treatment system and debt service on obligations of the Enterprise.

Coverage (1.00 required by covenant)	1.20

In 2001 the Enterprise issued an additional tier of revenue bonds. The bond covenants of the Junior Lien Variable Rate Demand Sewer Revenue Bonds, Series 2001A and Series 2001B, require that sewage disposal rates provide net revenue equal to at least 1.10 times the annual debt service requirements for all Junior Lien obligations after payment of senior lien requirements.

Coverage (1.10 required by covenant)	23.33