



**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)**

**Report of Independent Auditors and
Financial Statements with Required
Supplementary Information and
Supplemental Information**

December 31, 2011 and 2010

MOSS ADAMS LLP

Certified Public Accountants | Business Consultants

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REPORT OF INDEPENDENT AUDITORS

To the Director of Seattle Public Utilities
Drainage and Wastewater Fund
Seattle, Washington

We have audited the accompanying balance sheets of Seattle Public Utilities - Drainage and Wastewater Fund (the "Fund") as of December 31, 2011 and 2010, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Fund'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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 Seattle Public Utilities - Drainage and Wastewater Fund as of December 31, 2011 and 2010, 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 discussion and analysis is not part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. This information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements. The supplemental information following the financial statements is presented for purposes of additional analysis and is not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The supplemental information following the financial statements has not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Moss Adams LLP

Seattle, Washington
April 25, 2012

**SEATTLE PUBLIC UTILITIES -
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(An Enterprise Fund of the City of Seattle)
MANAGEMENT'S DISCUSSION AND ANALYSIS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

As management of Seattle Public Utilities ("SPU"), a department of the City of Seattle (the "City"), we offer readers of SPU's financial statements this narrative overview and analysis of the financial activities of the Drainage and Wastewater Fund (the "Fund") for the fiscal years ended December 31, 2011 and 2010. The revenues, expenses, assets, and liabilities of Seattle's drainage and wastewater system are recorded in the Drainage and Wastewater Fund, the functions of which are primarily supported by user fees and charges to customers. The financial situation of other aspects of Seattle City government, including other utility services and general government operations, are reported elsewhere.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Fund's financial statements. The financial statements include Management's Discussion and Analysis and basic financial statements with accompanying notes.

Basic Financial Statements - The basic financial statements of the Fund report information about the Fund using accounting methods similar to those used by private sector companies. These statements offer short-term and long-term financial information about its activities. The basic financial statements begin on page 12 of this report and are comprised of three components: (1) Balance Sheets, (2) Statements of Revenues, Expenses, and Changes in Net Assets, and (3) Statements of Cash Flows.

The Balance Sheets present information, as of December 31, 2011 and 2010, on all of the Fund's assets and liabilities, with the difference between the two reported as net assets. They also provide information about the nature and amounts of investments in resources (assets), obligations to the Fund's creditors (liabilities), and provide the basis for assessing the liquidity and financial flexibility of the Fund.

The Statements of Revenues, Expenses, and Changes in Net Assets present changes in the Fund's net assets for the years ended December 31, 2011 and 2010. All changes in net assets are reported when the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. These statements reflect the results of the Fund's operations for the years identified to provide information about the Fund's credit worthiness and its ability to successfully recover all its costs through service fees and other charges.

The Statements of Cash Flows are required to provide information about the Fund's cash receipts and cash payments during the years ended December 31, 2011 and 2010. To provide answers to questions about sources, uses, and impacts to cash, these statements report cash receipts, cash payments, and net changes in cash resulting from operations, investing and financing activities for the reporting period.

Notes to the Financial Statements - The notes are an integral part of the financial statements. They provide additional disclosures that are essential to a full understanding of the data provided in the financial statements, such as for certain estimates and financing details. The notes to the financial statements begin on page 17 of this report.

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FINANCIAL ANALYSIS

Increases or decreases in net assets may serve over time as a useful indicator of whether the Fund's financial position is improving or deteriorating. At December 31, 2011 and 2010, the Fund's assets exceeded liabilities, resulting in a surplus of total assets of \$270.3 million and \$252.3 million, respectively. In 2011, the Fund's overall position improved, with an increase in net assets of \$18.0 million (7.1%) as compared to an increase in net assets of \$5.9 million (2.4%) in 2010. The following summary balance sheets present the assets of the Fund and show the mix of liabilities and net assets used to acquire these assets:

SUMMARY BALANCE SHEETS

	2011	2010	2009
ASSETS			
Current assets	\$ 71,477,456	\$ 67,258,730	\$ 58,500,719
Capital assets, net	663,434,318	628,042,924	593,680,810
Other	<u>107,346,278</u>	<u>143,778,405</u>	<u>180,578,109</u>
Total assets	<u>842,258,052</u>	<u>839,080,059</u>	<u>832,759,638</u>
LIABILITIES			
Current liabilities	55,753,517	58,065,225	49,047,862
Revenue bonds	477,318,769	491,116,902	504,395,035
Other	<u>38,926,782</u>	<u>37,608,873</u>	<u>32,879,570</u>
Total liabilities	<u>571,999,068</u>	<u>586,791,000</u>	<u>586,322,467</u>
NET ASSETS			
Invested in capital assets, net of related debt	223,131,662	216,471,199	207,138,801
Restricted	28,383,412	28,099,086	26,200,782
Unrestricted	<u>18,743,910</u>	<u>7,718,774</u>	<u>13,097,588</u>
TOTAL NET ASSETS	<u>\$ 270,258,984</u>	<u>\$ 252,289,059</u>	<u>\$ 246,437,171</u>

2011 Compared to 2010

Assets - Current assets increased \$4.2 million (6.3%) over the prior year primarily due to increases totaling \$5.9 million in unbilled revenue, due from other governments and accounts receivable, net from the Combined Customer Service System. These increases were offset by decreases totaling \$1.7 million in cash and equity in pooled investments and due from other city funds.

Other assets decreased \$36.4 million (25.3%) due to the spending of \$40.4 million for use toward construction projects, reductions of \$0.7 million in deferred external infrastructure costs and a decrease in vendor deposits, and cash and equity in pooled investments of \$0.5 million. These decreases were impacted by increases totaling \$2.7 million in other restricted accounts, cash and equity in pooled investments mainly due to funding received for work toward the Alaskan Way Viaduct project and in notes and contracts receivable from the Public Infrastructure Agreement with the Seattle Housing Authority (see Note 11). In addition, the Fund experienced increases totaling \$2.6 million in deferred environmental costs and recoveries and other deferred charges, which primarily related to the 2010 Combined Sewer Overflow Plan. The projects identified in the plan will ultimately enhance the water quality of Lake Washington, Puget Sound, Elliott Bay, the Ship Canal, the Duwamish, Longfellow Creek, Lake Union, Union Bay, and Portage Bay.

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FINANCIAL ANALYSIS (Continued)

Liabilities - Current liabilities decreased \$2.3 million (4.0%) from 2010. This is mostly attributable to decreases in deferred credits, accounts payable and due to other city funds, totaling \$3.3 million, offset by an increase of \$1.0 million in due to other governments.

Noncurrent and other liabilities increased \$1.3 million (3.5%). This is due to an increase in Public Works Trust Fund loans (see Note 10), offset by a decrease in environmental liabilities (see Note 9).

Net Assets - The largest portion of the Fund's net assets (\$223.1 million or 82.6%) reflects the Fund's investment in capital assets such as land, buildings, and equipment, less any related outstanding debt used to acquire those assets. The Fund uses these assets to provide services to customers; consequently, these assets are not available for future spending. Although the Fund's investment in its capital assets is reported net of related debt, the resources needed to repay the debt are provided by fees paid by customers for services provided by these assets. In 2011, net assets invested in capital assets net of related debt increased \$6.7 million from 2010 due to an increase in capital assets placed in service, net of depreciation offset by the related debt.

The Fund's restricted net assets (\$28.4 million or 10.5%) represent resources that are subject to restrictions on how they may be used. This portion of net assets increased \$0.3 million from 2010. This change was primarily due to an increase in deferred charges related to the 2010 Combined Sewer Overflow Plan, less related debt.

The remaining portion of the Fund's net assets (\$18.7 million or 6.9%) represent resources that are unrestricted and may be used to meet the Fund's obligations to creditors. Unrestricted net assets increased \$11.0 million from 2010 in part due to the rate increase effective January 1, 2011.

2010 Compared to 2009

Assets - Current assets increased \$8.7 million (15.0%) over the prior year. This increase was primarily due to the use of bond proceeds for 2011 expenditures on CIP projects. In addition there were increases in accounts receivable, net from the Combined Customer Service System.

Other assets decreased \$36.8 million (20.4%) mainly due to the spending of \$40.6 million for use toward construction projects and a decrease in restricted interest receivables of \$0.5 million. These decreases were offset by an increase of \$4.3 million in deferred charges, which primarily related to the 2010 Combined Sewer Overflow Plan. The projects identified in the plan will ultimately enhance the water quality of Lake Washington, Puget Sound, Elliot Bay, the Ship Canal, the Duwamish, Longfellow Creek, Lake Union, Union Bay, and Portage Bay.

Liabilities - Current liabilities increased \$9.0 million (18.4%) from 2009. This is mostly attributable to a \$3.9 million increase in accounts payable to support the work involved with the Madison Valley Long Term Solution project and a \$1.7 million increase in due to other city funds for funding provided to the general fund for taxes and general judgments and claims. In addition, deferred credits and other increased \$1.7 million from customer billings and \$1.6 million from receipt of a contribution from the Seattle Department of Transportation for future work on the Alaskan Way Viaduct.

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FINANCIAL ANALYSIS (Continued)

Noncurrent and other liabilities increased \$4.7 million (14.4%). This is due to increases in Public Works Trust Fund loans (see Note 10), the noncurrent portion of claims payable (see Note 7), the noncurrent portion of compensated absences (see Note 8), and environmental liabilities (see Note 9).

Net Assets - The largest portion of the Fund's net assets (\$216.5 million or 85.8%) reflects the Fund's investment in capital assets such as land, buildings, and equipment, less any related outstanding debt used to acquire those assets. The Fund uses these assets to provide services to customers. Consequently, these assets are not available for future spending. Although the Fund's investment in its capital assets is reported net of related debt, the resources needed to repay the debt are provided by fees paid by customers for services provided by these assets. In 2010, net assets invested in capital assets net of related debt increased \$9.4 million from 2009 due to an increase in capital assets placed in service, net of depreciation offset by the related debt.

The Fund's restricted net assets (\$28.1 million or 11.1%) represent resources that are subject to restrictions on how they may be used. This portion of net assets increased \$1.9 million. This change was primarily due to an increase in deferred charges related to the 2010 Combined Sewer Overflow Plan, less related debt.

The remaining portion of the Fund's net assets (\$7.7 million or 3.1%) represent resources that are unrestricted and may be used to meet the Fund's obligations to creditors. Unrestricted net assets decreased approximately \$5.4 million primarily due to a higher percentage of capital projects funded with operating cash as compared to the prior year.

The following summary statements of revenues, expenses, and changes in net assets present the annual surplus of revenues over expenses (the change in net assets):

SUMMARY STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS

	2011	2010	2009
Operating revenues	\$ 278,956,907	\$ 249,733,794	\$ 250,194,607
Operating expenses	(253,071,273)	(230,118,012)	(230,823,698)
Net operating income	25,885,634	19,615,782	19,370,909
Other income (expenses)	(18,239,166)	(16,894,597)	(17,240,103)
Fees, contributions, and grants and special items	10,323,457	3,130,703	4,140,738
Change in net assets	<u>\$ 17,969,925</u>	<u>\$ 5,851,888</u>	<u>\$ 6,271,544</u>

2011 Compared to 2010

Current year operating revenues increased approximately \$29.2 million (11.7%) from 2010. This is primarily due to a \$20.2 million increase in wastewater revenues resulting from an average increase in rates of 14.5% and a \$9.4 million increase in drainage revenues due to increased rates. These increases were offset by a decrease of \$0.6 million in system usage.

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FINANCIAL ANALYSIS (Continued)

Operating expenses increased \$23.0 million (10.0%) from 2010. Notable factors affecting this change include increases in wastewater treatment of \$14.0 million due to an increase in the treatment rate imposed by King County in 2011. Additional increases to expenses include \$4.9 million in the utility systems management branch related to the abandonment of the Densmore Basin project and the unsuccessful Ballard rain gardens project. Finally, city and other tax expenses increased \$3.8 million related to the overall increase in revenue.

Other income (expenses), increased \$1.3 million from 2010. Factors impacting this change were lower environmental cost recoveries and insurance recoveries totaling \$2.7 million. These factors were offset by an additional \$1.0 million in interest expense for capitalized interest costs related to construction projects and higher Build America Bond interest income of \$0.3 million.

Fees, contributions, and grants and special items increased \$7.2 million due to infrastructure assets donated by the Seattle Department of Transportation, as well as, revenue from the Seattle Housing Authority, Sound Transit and the Alaskan Way Viaduct project. In addition, the Fund had a decrease in environmental remediation expenses.

2010 Compared to 2009

Prior year operating revenues decreased approximately \$0.5 million (0.2%). This is due to an overall \$1.7 million decrease in other operating revenue related primarily to a \$1.4 million decrease in other engineering services. This decrease was offset by a \$0.9 million increase in wastewater revenues due to an average increase in rates of 5.2% offset by a 1.0% decrease in system usage.

Operating expenses decreased \$0.7 million (0.3%). Notable factors affecting this change include decreases in branch spending of \$3.2 million for the field operations, project delivery, and customer service branches. These decreases were offset by increases in the utility systems management branch of \$0.3 million, claims expense in the general and administrative branch of \$1.6 million, and an increase in city and other tax expenses of \$0.6 million.

Other income (expenses), decreased \$0.3 million. Factors impacting this change include an environmental cost recovery of \$2.4 million. Further, Build America Bond interest income from the 2009 bond issuance totaled \$1.6 million and an insurance recovery totaled \$0.3 million. These factors were offset by an additional \$4.0 million in interest expense for bonded debt.

Fees, contributions, and grants and special items decreased \$1.0 million (24.4%) primarily due to revenue from the Seattle Housing Authority received in 2009, which did not occur in 2010, offset by a decrease in environmental remediation costs.

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CAPITAL ASSETS

The following table summarizes capital assets, net of accumulated depreciation, by major asset category:

SUMMARY OF CAPITAL ASSETS, NET OF ACCUMULATED DEPRECIATION

	2011	2010	2009
Land and land rights	\$ 14,279,516	\$ 14,279,516	\$ 11,090,693
Buildings	7,745,381	8,017,345	8,135,837
Structures	114,758,607	101,910,764	99,346,669
Machinery and equipment	450,664,575	424,460,591	406,794,994
Computer systems	12,492,853	13,640,712	12,638,307
Construction in progress	62,822,427	65,071,758	55,054,703
Other property	670,959	662,238	619,607
Capital assets, net of accumulated depreciation	<u>\$ 663,434,318</u>	<u>\$ 628,042,924</u>	<u>\$ 593,680,810</u>

2011 Compared to 2010

The Fund's investment in capital assets, net of accumulated depreciation, for the year ended December 31, 2011 was \$663.4 million. This represented an increase of approximately \$35.4 million (5.6%) compared to 2010. Highlights of the Fund's major capital assets placed in service during 2011 included the following:

- \$26.2 million for the completion of the Madison Valley Phase II project.
- \$4.7 million to replace sewer pipelines throughout several locations within the city.
- \$4.2 million in donated sewer and drainage pipes from the Seattle Department of Transportation.
- \$3.1 million in improvements related to stormwater quality conditions in the Norfolk Basin.
- \$1.4 million in emergency rehabilitation work on sewer mainlines.
- \$1.2 million for I-SCADA improvements at wastewater pump stations.
- \$1.2 million to reduce infiltration and enhance the capacity of the sewer at 12th Avenue NW.
- \$1.1 million for the installation of onsite generators at critical wastewater pump stations.

Highlights of the Fund's major construction projects in progress at the end of 2011 include the following:

- \$16.2 million for improvements to the Windermere combined sewer overflow storage.
- \$8.2 million for improvements to the South Henderson combined sewer overflow storage.

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CAPITAL ASSETS (Continued)

- \$5.9 million for a detention project to reduce flooding near North 107th Street and Midvale.
- \$5.9 million to build a pump station and a water quality facility near 7th and Riverside in South Park.
- \$3.8 million for improvements to the South Genesee combined sewer overflow facilities.
- \$3.7 million for the relocation and replacement of wastewater related facilities in the Mercer Corridor.
- \$1.8 million in Capital Hill water quality improvements.
- \$1.1 million to upgrade the Maximo system.
- \$1.1 million to review conceptual designs, business case development, negotiation of agreements, and project management related to the Alaskan Way Viaduct bored tunnel project.

2010 Compared to 2009

The Fund's investment in capital assets, net of accumulated depreciation, for the year ended December 31, 2010 was \$628.0 million. This represented an increase of approximately \$34.4 million (5.8%) compared to 2009. Highlights of the Fund's major capital assets placed in service during 2010 included the following:

- \$5.2 million to replace sewer pipelines throughout several locations within the city.
- \$3.9 million for storm improvements to replace undersized pipes along Martin Luther King Way and Norfolk Street.
- \$3.2 million for the completion of Madison Valley Phase I and the purchase of land in conjunction with the project.
- \$2.9 million to replace existing pipes along the Alaskan Way Viaduct and Seawall with improved earthquake resistant structures.
- \$2.6 million in emergency rehab work on sewer mainlines.
- \$2.1 million for storm improvements at 30th and Johns Street.
- \$1.6 million for culvert repairs at NE 105th and 17th.
- \$1.5 million for major enhancements to the I-SCADA data management program and IMS web site portal application.

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CAPITAL ASSETS (Continued)

- \$1.5 million for wastewater and pump station improvements and rehabilitation.
- \$1.1 million in donated sewer and drainage pipes from Seattle Department of Transportation and Sound Transit.

Highlights of the Fund's major construction projects in progress at the end of 2010 included the following:

- \$6.9 million for improvements to mitigate flooding and sewer backups at the storm water facility in Madison Valley.
- \$5.1 million for a detention project to reduce flooding near North 107th Street and Midvale.
- \$4.4 million to build a pump station and a water quality facility near 7th and Riverside in South Park.
- \$3.0 million for improvements to the Windermere combined sewer overflow storage.
- \$1.8 million for improvements to the South Henderson combined sewer overflow storage.
- \$1.8 million for improvements to the South Genesee combined sewer overflow facilities.
- \$1.7 million to evaluate stormwater quality conditions in the Norfolk Basin.

Additional information about the Fund's capital assets can be found in Note 3 of this report.

DEBT ADMINISTRATION

The Fund's debt primarily consists of bonded debt and public works trust fund loans. Bonded debt is secured solely by drainage and wastewater system revenues and provides financing for capital improvements. Public works trust loans are unsecured loans issued by the Washington State Department of Commerce for certain capital improvements. The Fund's credit ratings on its bonds were AA+ by Standard and Poor's Rating Service and Aa1 by Moody's Investor Service.

2011 Compared to 2010

At the end of 2011, the Fund had \$486.6 million in bonded debt, as compared to \$499.8 million in 2010, all of which was secured solely by drainage and wastewater system revenues. There were no new bonds issued in 2011. Additional information about the Fund's long-term debt can be found in Notes 4 and 10.

During 2011, the Fund made additional draws on public works trust fund loans. The Fund borrowed an additional \$3,574,418 from the Washington State Department of Commerce and the Fund also borrowed \$228,682 from the Washington State Department of Ecology, which was funded by the American Recovery and Reinvestment Act of 2009 (ARRA) (see Note 10).

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DEBT ADMINISTRATION (Continued)

2010 Compared to 2009

At the end of 2010, the Fund had \$499.8 million in bonded debt, as compared to \$513.1 million in 2009, all of which was secured solely by drainage and wastewater system revenues. There were no new bonds issued in 2010.

During 2010, the Fund made additional draws on public works trust fund loans. The Fund borrowed an additional \$170,000 from the Washington State Department of Commerce and \$359,363 from the Washington State Department of Ecology. This loan was funded by the American Recovery and Reinvestment Act of 2009 (ARRA) (see Note 10).

REQUESTS FOR INFORMATION

The Fund's financial statements are designed to provide a general overview of the Fund's finances, as well as to demonstrate the Fund's accountability to its customers, investors, creditors, and other interested parties. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Seattle Public Utilities, Finance and Administration Branch, Finance Division, PO Box 34018, Seattle, Washington 98124-4018, telephone: (206) 684-3000.

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BALANCE SHEETS
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ASSETS	2011	2010
CURRENT ASSETS		
Cash and equity in pooled investments	\$ 29,121,787	\$ 30,284,181
Bond parity account, restricted cash and equity in pooled investment	1,571,461	1,619,724
Accounts receivable, net of allowance for doubtful accounts of \$1,866,543 and \$1,490,824, respectively	19,951,276	16,982,980
Unbilled revenues	15,914,459	14,226,363
Due from other City funds	1,870,874	2,410,515
Due from other governments	2,344,910	1,032,752
Materials and supplies inventory	570,165	608,523
Prepayments and other	132,524	93,692
Total current assets	<u>71,477,456</u>	<u>67,258,730</u>
RESTRICTED ASSETS		
Bond reserve account, cash and equity in pooled investments	12,777,456	12,769,423
Construction fund		
Cash and equity in pooled investments	36,123,278	51,572,451
Dedicated investments	-	24,943,188
Interest receivable	-	125,426
Other restricted accounts, cash and equity in pooled investments	1,441,148	-
Vendor deposits, cash and equity in pooled investments	13,611	527,241
Total restricted assets	<u>50,355,493</u>	<u>89,937,729</u>
DEFERRED CHARGES AND OTHER		
Unamortized bond issue costs	3,089,486	3,228,093
Notes and contracts receivable	1,306,324	-
Deferred external infrastructure costs	20,577,735	21,270,289
Deferred environmental costs and recoveries	7,398,798	7,180,984
Other deferred charges	24,618,442	22,161,310
Total deferred charges and other	<u>56,990,785</u>	<u>53,840,676</u>
CAPITAL ASSETS		
Capital assets, excluding land	831,908,520	776,878,196
Less accumulated depreciation	(246,247,104)	(228,848,784)
	<u>585,661,416</u>	<u>548,029,412</u>
Construction in progress	62,822,427	65,071,758
Land and land rights	14,279,516	14,279,516
Other property	670,959	662,238
Total capital assets	<u>663,434,318</u>	<u>628,042,924</u>
TOTAL ASSETS	<u><u>\$ 842,258,052</u></u>	<u><u>\$ 839,080,059</u></u>

**SEATTLE PUBLIC UTILITIES -
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BALANCE SHEETS (CONTINUED)
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	LIABILITIES AND NET ASSETS	
	2011	2010
CURRENT LIABILITIES		
Accounts payable	\$ 8,637,576	\$ 9,036,993
Accrued payroll and payroll taxes payable	1,401,256	1,265,767
Taxes payable	246,344	245,728
Interest payable	6,451,933	6,587,144
Due to other City funds	4,696,918	6,603,770
Due to other governments	10,339,097	9,252,282
Claims payable	3,459,286	3,468,383
Environmental liabilities	2,263,979	2,839,874
Compensated absences payable	374,356	355,705
Revenue bonds due within one year	13,695,000	13,175,000
Loans due within one year	903,774	814,130
Deferred credits and other	3,283,998	4,420,449
Total current liabilities	<u>55,753,517</u>	<u>58,065,225</u>
REVENUE BONDS		
Revenue bonds, due serially	486,610,000	499,785,000
Less revenue bonds due within one year	(13,695,000)	(13,175,000)
Bond discounts	(1,077,502)	(1,123,061)
Bond premiums	9,633,210	10,055,705
Loss on refunding	(4,151,939)	(4,425,742)
Total revenue bonds	<u>477,318,769</u>	<u>491,116,902</u>
NONCURRENT AND OTHER LIABILITIES		
Vendor deposits payable	13,611	527,241
Compensated absences payable	4,050,598	3,926,874
Other postemployment benefits	1,894,828	1,378,711
Claims payable	8,830,523	9,133,451
Loans	17,693,988	14,809,874
Environmental liabilities	6,291,846	7,760,059
Other noncurrent liabilities	151,388	72,663
Total noncurrent and other liabilities	<u>38,926,782</u>	<u>37,608,873</u>
Total liabilities	<u>571,999,068</u>	<u>586,791,000</u>
NET ASSETS		
Invested in capital assets, net of related debt	223,131,662	216,471,199
Restricted	28,383,412	28,099,086
Unrestricted	18,743,910	7,718,774
Total net assets	<u>270,258,984</u>	<u>252,289,059</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 842,258,052</u>	<u>\$ 839,080,059</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)**
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
OPERATING REVENUES		
Direct service	\$ 274,224,369	\$ 244,947,310
Other	4,732,538	4,786,484
Total operating revenues	<u>278,956,907</u>	<u>249,733,794</u>
OPERATING EXPENSES		
Wastewater treatment	125,251,546	111,282,206
Utility systems management	16,574,074	14,475,619
Field operations and maintenance	18,873,873	18,553,795
Project delivery	11,368,181	8,589,280
Customer services	5,207,443	4,738,617
Pre-capital planning and development	2,565,065	1,132,929
General and administrative	17,367,886	18,937,703
City taxes	32,448,908	29,177,471
Other taxes	3,582,168	3,099,045
Depreciation and amortization	19,832,129	20,131,347
Total operating expenses	<u>253,071,273</u>	<u>230,118,012</u>
NET OPERATING INCOME	<u>25,885,634</u>	<u>19,615,782</u>
OTHER INCOME (EXPENSES)		
Investment income	2,820,139	2,595,478
Interest expense	(21,129,394)	(22,608,323)
Amortization of bond premiums	376,936	376,936
Amortization of bond refunding loss	(273,803)	(273,803)
Amortization of debt issuance costs	(138,607)	(138,607)
Gain (loss) on disposition of capital assets	12,901	(27,289)
Other, net	92,662	3,181,011
Total other expenses	<u>(18,239,166)</u>	<u>(16,894,597)</u>
FEES, CONTRIBUTIONS, AND GRANTS AND SPECIAL ITEMS		
Capital fees, contributions, and grants	7,475,683	3,822,548
Operating fees, contributions, and grants	2,309,750	1,256,310
Environmental remediation	538,024	(1,948,155)
Total fees, contributions, and grants and special items	<u>10,323,457</u>	<u>3,130,703</u>
CHANGE IN NET ASSETS	<u>17,969,925</u>	<u>5,851,888</u>
NET ASSETS		
Beginning of year	<u>252,289,059</u>	<u>246,437,171</u>
End of year	<u>\$ 270,258,984</u>	<u>\$ 252,289,059</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	\$ 271,464,707	\$ 251,065,796
Cash paid to suppliers	(148,849,754)	(126,922,634)
Cash paid to employees	(49,700,928)	(46,039,524)
Cash paid for taxes	(35,822,166)	(29,754,787)
Net cash provided by operating activities	<u>37,091,859</u>	<u>48,348,851</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Operating grants received	2,204,999	1,186,505
Environmental remediation outflows	(2,848,308)	(2,794,071)
Other nonoperating cash inflows	1,308,380	4,358,057
Other nonoperating cash outflows	(15,145)	(27,303)
Net cash provided by noncapital financing activities	<u>649,926</u>	<u>2,723,188</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from loans	3,818,263	2,846,570
Capital fees, contributions, and grants	2,938,786	2,726,656
Principal payments on revenue bonds	(13,175,000)	(13,285,000)
Principal payments on loans	(844,505)	(533,467)
Capital expenditures and deferred charges	(49,442,364)	(55,569,549)
Interest paid on long-term debt	(24,307,874)	(24,105,731)
Proceeds from sale of capital assets	111,858	49,322
Net cash used in capital and related financing activities	<u>(80,900,836)</u>	<u>(87,871,199)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	-	(34,400,000)
Proceeds from sales of investments	24,600,000	108,600,000
Interest received on investments	2,834,772	2,573,687
Net cash provided by investing activities	<u>27,434,772</u>	<u>76,773,687</u>
NET (DECREASE) INCREASE IN CASH AND EQUITY IN POOLED INVESTMENTS	(15,724,279)	39,974,527
CASH AND EQUITY IN POOLED INVESTMENTS		
Beginning of year	<u>96,773,020</u>	<u>56,798,493</u>
End of year	<u>\$ 81,048,741</u>	<u>\$ 96,773,020</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
STATEMENTS OF CASH FLOWS (CONTINUED)
YEARS ENDED DECEMBER 31, 2011 AND 2010**

	2011	2010
RECONCILIATION OF NET OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Net operating income	\$ 25,885,634	\$ 19,615,782
Adjustments to reconcile net operating income to net cash provided by operating activities		
Depreciation and amortization	19,832,129	20,131,347
Changes in operating assets and liabilities		
Accounts receivable	(2,968,296)	(2,391,175)
Unbilled revenues	(1,688,096)	343,003
Due from other City funds	539,641	(833,240)
Due from other governments	(984,235)	854,113
Materials and supplies	38,358	(60,527)
Other assets	(8,775)	(5,481)
Vendor deposits payable	(434,904)	(160,318)
Notes and contracts receivable	(1,351,014)	-
Accounts payable	(399,418)	3,972,421
Accrued payroll and payroll taxes payable	135,489	145,174
Taxes payable	616	(66,355)
Compensated absences payable	142,375	458,304
Other postemployment benefits	516,117	405,349
Due to other City funds	(1,906,852)	1,675,465
Due to other governments	1,086,815	(3,672)
Claims payable	(312,025)	900,844
Deferred credits and other liabilities	(1,031,700)	3,367,817
Total adjustments	<u>11,206,225</u>	<u>28,733,069</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 37,091,859	\$ 48,348,851
NONCASH TRANSACTIONS		
Change in fair value of investments	\$ (4,085)	\$ (42,763)
Contributed infrastructure	<u>4,208,974</u>	<u>1,095,892</u>
Total noncash transactions	<u>\$ 4,204,889</u>	<u>\$ 1,053,129</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies

Operations - The City of Seattle, Seattle Public Utilities - Drainage and Wastewater Fund (the "Fund") is a public utility enterprise fund of the City of Seattle (the "City"). The Fund was established to account for the drainage and wastewater activities of Seattle Public Utilities ("SPU"). Drainage activities include regulating storm water runoff, alleviating flooding, mitigating water pollution caused by runoff, and responding to federal storm water regulations, in addition to managing drainage utility assets. Wastewater activities consist of managing the City's sewer system, including the operation of sewer utility facilities and pumping stations necessary to collect the sewage of the City and discharge it into the King County Department of Natural Resources Wastewater Treatment System for treatment and disposal.

On January 1, 1997, the City created SPU, which brought together under one administrative umbrella the water, solid waste, and drainage and wastewater functions of the City. The Fund (as well as SPU's other funds) remains separate for accounting purposes.

SPU receives certain services from other departments and agencies of the City, including some that are normally considered to be general and administrative. The Fund is charged a share of these costs and additionally pays a business and occupation tax to the City's General Fund. During 2011 and 2010, the Fund paid \$8,739,578 and \$8,224,907, respectively, to the City for its share of general and administrative services. Additionally, the Fund paid \$32,448,908 and \$29,177,471 to the City for business and occupation utility taxes in 2011 and 2010, respectively.

Wastewater disposal services provided to other City departments and agencies are billed at rates prescribed by City ordinances. The Fund collected \$1,852,250 in 2011 and \$1,776,680 in 2010 from the City for wastewater services provided.

The utility billing function is co-managed by both SPU and Seattle City Light ("SCL"). SPU provides customer service through the call center and walk-in center. SCL operates and manages the billing system, Combined Customer Services System ("CCSS"). SPU and SCL bills and reimburses each other for these services. Within SPU, the costs and reimbursements were shared among its three utility funds (Water, Drainage and Wastewater, and Solid Waste). The Fund received reimbursements related to the call center and walk-in center of \$1,396,068 and \$1,589,558 in 2011 and 2010, respectively. The Fund paid \$384,365 and \$307,173 for CCSS services in 2011 and 2010, respectively, which does not include reimbursements to SCL for the Fund's share of capital costs to upgrade the CCSS system.

The Fund is subject to regulation by the City and the state of Washington. Service rates are authorized by ordinances passed by the City Council. Accounting policies and financial reporting are regulated by the Washington State Auditor's Office, and conform to accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board ("GASB") is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The Fund has chosen to apply all pronouncements and interpretations issued by the GASB, as well as those issued by the Financial Accounting Standards Board ("FASB") on or before November 30, 1989, except when they conflict with the GASB.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies (Continued)

Basis of Accounting - The Fund is accounted for on a flow of economic resources measurement focus. Its' 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. With the flow of economic resources measurement focus, all assets and liabilities associated with the Fund's operations are included on the balance sheet. The operating statements present increases (revenues) and decreases (expenses) in total net assets.

Cash and Equity in Pooled Investments - Cash resources of the Fund are combined with cash resources of the City to form a pool of cash that is managed by the City's Finance and Administration Services Department. Under the City's investment policy, the Finance and Administration Services Department invests all temporary cash surpluses either directly or through a "sweep account." Interest earned on the pooled investments is prorated to individual funds at the end of each month on the basis of their average daily cash balances during the month when interest was earned. The Fund's share of the pool is included in the accompanying Balance Sheets under the caption "cash and equity in pooled investments." The pool operates like a demand deposit account in that all City departments may deposit cash at any time and can also withdraw cash out of the pool without prior notice or penalty. Accordingly, the Statements of Cash Flows reconcile to cash and equity in pooled investments. Cash and equity in pooled investments are reported at fair value.

Investments - The Fund's restricted cash resources are invested by the Finance and Administration Services Department separate from the cash and investments pool. Investments are managed in accordance with the City's investment policy, with limits and restrictions applied at the City-wide level rather than to specific investments of the Fund. These investments are reported at fair value.

Receivables and Unbilled Revenues - Customer accounts receivable consist of amounts owed by private individuals and organizations for goods delivered or services rendered in the regular course of business operations. Receivables are shown net of allowances for doubtful accounts. The Fund also accrues an estimated amount for services that have been provided but not billed.

Activity between funds that is outstanding at the end of the year, not related to the provision of utility services, is reported as due from other funds.

Allowance for Doubtful Accounts - A reserve has been established for uncollectible accounts receivable based on actual historical write-off trends and knowledge of specific circumstances that indicate collection of an account may be unlikely.

Materials and Supplies Inventory - The Fund values its inventory based on a moving average method. The most recent total cost of an inventory item is divided by the total units of the item that remain in inventory to determine the moving average cost of the item. The moving average cost is then applied to all the units of the inventory item.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies (Continued)

Restricted Assets - The construction fund accounts are comprised of unexpended bond proceeds, a portion of which is scheduled to be spent in 2012.

Unamortized Bond Issue Costs - Costs associated with the issuance of bonds are amortized to expense over the term of the related debt. Amortization expense is calculated using the straight line method.

Deferred External Infrastructure Costs - The Fund has contributed \$21,962,828 to a joint project with King County to expand one of their transmission lines to help alleviate sewer overflows in the area. These costs represent the portion of the project that did not result in an asset for the Fund. The project was completed in 2005. The Fund has deferred these costs and began amortizing them in 2006 over a 75 year period.

Environmental Remediation Costs - The Fund is involved in several remediation efforts around the City (see Note 9). When estimated remediation costs are approved to be recovered through rates, the costs associated with these efforts are deferred when accrued and are amortized over the rate recovery period. Certain environmental remediation costs that are infrequent in occurrence are treated as a special item in the Statements of Revenues, Expenses, and Changes in Net Assets.

Other Deferred Charges - Other deferred charges primarily include costs related to leasehold improvements and plans, such as the Combined Sewer Overflow Update plan and the Comprehensive Ditch and Culvert plan. The Fund amortizes these charges over a 5 to 30 year period.

Capital Assets - Capital assets are stated at cost or, if contributed, at fair value at the date of contribution. Costs include direct material, labor, and indirect costs such as engineering, supervision, payroll taxes, pension benefits, and interest relating to the financing of projects under construction. The cost of current repairs and maintenance is charged to expense, while the cost of additions and improvements is capitalized. SPU's policy is to generally capitalize assets with a cost of \$5,000 or more. The Fund received donated assets, such as sewer and drainage pipes, from developers and other government agencies.

Construction in Progress - Capitalizable costs incurred on projects which are not in use or ready for use are held in construction in progress. When the asset is ready for use, related costs are transferred to capital assets. Upon determining that a project will be abandoned, the related costs are charged to expense.

Other Property - Other property is stated at cost, or if contributed, the fair value at the date of contribution. Other property includes artwork and property held for future use. The artwork is acquired through the City's "One Percent for Art" program, which supports the City ordinance established to direct the inclusion of works of art in public spaces within the City.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies (Continued)

Depreciation - Capital assets in service are depreciated on the straight-line method over estimated useful lives as follows:

Buildings and fixtures	10 - 50 years
Laterals, mains, and outfalls	75 years
Detention structures	50 years
Pumping stations, equipment, and overflow structures	10 to 50 years
Machinery and equipment	3 to 20 years
Computer systems	3 to 10 years

Composite rates based on year of addition are used for depreciating the laterals, mains, and outfalls asset group. For most assets, it is SPU's policy to begin depreciation in the year following acquisition and to record a full year's depreciation in the year of disposition. This does not apply to heavy equipment, for which depreciation begins in the month following the equipment's in-service date to more accurately allocate equipment costs to various activities.

Environmental Liabilities - The Fund has accrued a liability for pollution remediation activities in accordance with GASB Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*. GASB 49 outlines five specific obligating events that give rise to estimating expected pollution remediation outlays. These outlays may be accrued as a liability and expensed, or if appropriate, capitalized.

The Fund will accrue a liability if any of the following obligating events occurs:

- The Fund is compelled to take pollution remediation action because of an imminent endangerment.
- The Fund violates a pollution prevention-related permit or license.
- The Fund is named, or evidence indicates it will be named, by a regulator as a potentially responsible party ("PRP") for remediation.
- The Fund is named, or evidence indicates that it will be named, in a lawsuit to compel participation in pollution remediation.
- The Fund commences or legally obligates itself to commence pollution remediation.

Most pollution remediation outlays do not qualify for capitalization and the Fund does not anticipate significant capitalized costs in the future. See Note 9 for site descriptions.

Compensated Absences - Employees earn vacation based upon their date of hire and years of service, and may accumulate earned vacation up to a maximum of 480 hours. Unused vacation at retirement or normal termination is considered vested and payable to the employee. Earned but unused vacation is accrued as a liability of the Fund. Employees also earn up to 12 days of sick leave per year and may accumulate sick leave balances without limit.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies (Continued)

Employees who submit the required documentation to be represented by the Coalition of City Unions are paid 35% of the value of unused sick leave upon retirement as part of the Health Reimbursement Arrangement – Voluntary Employees’ Beneficiary Association (“HRA-VEBA”) program. If the employee fails to submit the required documentation by their last working day of employment, their sick leave balance is forfeited.

Retiring employees who are not eligible to participate in the HRA-VEBA program may elect to receive 25% of the value of unused sick leave upon retirement or defer receipt of 35% of the value of their sick leave balance to the City’s 457 Plan and Trust, subject to the year-to-date or life-to-date limitations on deferrals and contributions. If the 35% value of the sick leave balance exceeds the maximum amount deferred to the City’s 457 Plan and Trust, the employee shall receive a taxable cash payment equal to the amount by which the 25% value of the sick leave balance exceeds the 35% that was allowed to be deferred. The Fund records a liability for estimated sick leave payments.

Operating Revenues - Wastewater service revenues are recorded through cycle billings rendered to customers monthly or bimonthly. The Fund accrues and records unbilled wastewater service revenues in the financial statements for services provided from the date of the last billing to year end.

Drainage service charges are billed to the City’s drainage residential and nonresidential customers twice a year through the service of King County’s property tax billing system. These charges fund operations and maintenance of, and improvements to, the City’s system of storm and drainage facilities.

Other operating revenues include revenues generated from wastewater and sewer permits, and engineering services provided to other City funds.

Operating Expenses - Certain expenses of the Fund are reported on the income statement by functional category. The types of work performed within each category are as follows:

- Pre-capital planning and development - Provides planning services and other related costs prior to the start of capital projects.
- Utility systems management - Accounts for the overall management of the Fund’s infrastructure assets, assuring they are properly designed, constructed, operated, and protected.
- Field operations - Operates and maintains the Fund’s drainage and wastewater systems.
- Project delivery - Provides project management and engineering services to the Fund and executes the Fund’s capital projects from start to completion.
- Customer services - Invoices the Fund’s customers for services provided and is the primary point of contact for customers.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies (Continued)

Taxes - The Fund is charged a public utility tax by the City at a rate of 12.0% for Wastewater revenues and 11.5% for Drainage revenues, net of certain credits. In addition, the Fund paid a 3.85% public utility tax to the State on a certain portion of revenues identified as sewer collection revenues. The Fund also paid business and occupation tax to the State at the rate of 1.8% on certain other non-utility revenues.

Other Revenues and Expenses - This includes the non-operating revenues and expenses that arise from transactions not related directly to the major income-earning operations of the Fund and are of a recurring nature. Major items are investment and interest income, interest expense, amortization of debt expenses, and sale of capital assets.

Net Assets - The Balance Sheet reports all financial and capital resources. The difference between assets and liabilities is net assets. There are three components of net assets: invested in capital assets - net of related debt, restricted, and unrestricted.

Invested in capital assets, net of related debt, consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Net assets are restricted when constraints placed on net asset use are either: (1) externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or (2) imposed by law through constitutional provisions or enabling legislation. The Fund's restricted net assets as of December 31, 2011 and 2010 are related to the bond debt reserve funds and certain deferred charges. Unrestricted net assets are those that are not "invested in capital assets, net of related debt" or "restricted."

Arbitrage Rebate Requirement - The Fund is subject to the Internal Revenue Code ("IRC"), Section 148(f), related to its tax-exempt revenue bonds. The IRC requires that earnings on gross proceeds of any revenue bonds that are in excess of the amount prescribed be surrendered to the Internal Revenue Service. As such, the Fund would record such a rebate as a liability. The Fund had no liability for arbitrage as of December 31, 2011 and 2010.

Accounting Changes - The Fund adopted GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, as of January 1, 2010. This statement clarified the definition of intangible assets as used in the description of capital assets in GASB Statement No. 34. The adoption of GASB 51 did not have a significant impact on the Fund's financial statements for 2011 or 2010.

The Fund adopted GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, as of January 1, 2010. This statement provides guidance for the recognition, measurement and disclosure of activity related to derivative instruments held by state and local governments. The adoption of GASB 53 did not have a significant impact on the Fund's financial statements for 2011 or 2010.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 1 - Operations and Summary of Significant Accounting Policies (Continued)

GASB issued Statement No. 59 *Financial Instruments Omnibus*, to update and improve existing financial reporting and disclosure standards of certain financial instruments and external investment pools. This statement became effective for periods beginning after June 15, 2010 and did not have a significant impact on the Fund's financial statements for 2011 or 2010.

GASB has issued Statement No. 62, *Codification of Pre-November 30, 1989 FASB Pronouncements*. This statement combines the authoritative accounting and financial reporting of the FASB and the American Institute of Certified Public Accountants ("AICPA"). The statement will eliminate the need for financial statement preparers and auditors to determine which FASB and AICPA pronouncement provisions apply to state and local governments. The statement is effective for periods beginning after December 15, 2011 and will not have a significant impact on the Fund's financial statements.

GASB has issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The requirements of this statement will standardize the presentation of deferred inflows and outflows of resources, and their effects on a government's net position. The statement is effective for periods beginning after December 15, 2011. The Fund is evaluating the impact of this standard on the financial statements.

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 amounts reported in the financial statements. Estimates and assumptions are used to record unbilled revenues, allowance for doubtful accounts, accrued sick leave, capitalized interest, depreciation, environmental liabilities, risk liabilities, and other contingencies. Changes in these estimates and assumptions may have a material impact on the financial statements.

Significant Risks and Uncertainties - The Fund is subject to certain business risks that could have a material impact on future operations and financial performance. These risks include, but are not limited to, weather and natural disaster-related disruptions, collective bargaining labor disputes, Environmental Protection Agency regulations, and federal government regulations or orders concerning the operation, maintenance, and licensing of facilities.

Reclassifications - Certain reclassifications have been made to prior year balances to provide a presentation consistent with the current year.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 2 - Cash and Investments

Custodial Credit Risk - Deposits - As of December 31, 2011 and 2010, the City's pool contained cash on deposit with the City's custodial banks in the amounts of \$19,666,051 and \$16,663,123, respectively. The deposits in excess of \$250,000 in both 2011 and 2010 were uninsured and uncollateralized. As such, these deposits were exposed to custodial credit risk, which is the risk that the deposits may not be returned to the City in the event of a bank failure. The City attempts to minimize exposure to custodial credit risk for deposits by requiring the depository bank to have sufficient capital to support the activity of the City. In addition, banks having a deposit relationship with the City are required to provide financial statements for the City's use in reviewing the bank's financial condition.

All deposits not covered by FDIC insurance are under the regulation of the Washington State Public Deposit Protection Commission (the "Commission") established in RCW 39.58 for public depository financial institutions. The Commission requires a pledge agreement and a trustee for each public depository financial institution. The trustee ensures eligible collateral defined as securities and designated for the benefit of public depositors, as described in RCW 39.58.050 (5) and (6), are segregated from all other assets. Eligible collateral is utilized by the trustee when the Commission has determined a loss, net of deposit insurance, has been incurred by a public depository financial institution.

Investments - As of December 31, the Fund's dedicated investments, the City's pooled investments, and dedicated investments of other funds were as follows:

2011					
	Dedicated Investments of the Fund	City Pool	Other Dedicated Investments	Total	Weighted Average Maturity (Days)
U.S. Government Agencies	\$ -	\$ 991,128,738	\$ -	\$ 991,128,738	974
State and Local Governments	-	105,403,511	-	105,403,511	513
Commercial Paper	-	77,494,937	-	77,494,937	10
Repurchase Agreements	-	66,785,435	-	66,785,435	3
U.S. Government Obligations	-	37,993,718	-	37,993,718	816
Total	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
			Portfolio Weighted Average Maturity		823
2010					
	Dedicated Investments of the Fund	City Pool	Other Dedicated Investments	Total	Weighted Average Maturity (Days)
U.S. Government Agencies	\$ 24,943,188	\$ 628,004,011	\$ 56,590,968	\$ 709,538,167	655
Commercial Paper	-	256,364,545	-	256,364,545	21
Repurchase Agreements	-	56,365,904	-	56,365,904	3
U.S. Government Obligations	-	39,624,611	-	39,624,611	398
State and Local Governments	-	1,020,110	-	1,020,110	213
Total	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
			Portfolio Weighted Average Maturity		458

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
(An Enterprise Fund of the City of Seattle)
NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 2 - Cash and Investments (Continued)

As of December 31, the Fund's share of the City pool was as follows:

	<u>2011</u>	<u>2010</u>
Cash and equity in pooled investments	\$ 29,121,787	\$ 30,284,181
Restricted cash and equity in pooled investments	<u>51,926,954</u>	<u>66,488,839</u>
Total	<u>\$ 81,048,741</u>	<u>\$ 96,773,020</u>
Balance as a percentage of City pool cash and investments	6.2%	9.7%

Interest Rate Risk - Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. In general, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The City manages this risk by limiting the average maturity of investments to five years. However, the Fund's investments are selected for greater liquidity in order to support the Fund's cash flow needs and therefore typically have much shorter average maturities.

Credit Risk - Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. In accordance with the City's investment policy, investments in commercial paper purchased on the secondary market are limited to those with maturities not longer than 180 days from purchase and with the highest rating by at least two nationally recognized statistical rating organizations ("NRSROs"). As of December 31, 2011 and 2010, the City's investments in commercial paper were rated P-1 by Moody's Investors Service and A-1 or A-1+ by Standard & Poor's Rating Service.

The City also purchases obligations of government-sponsored enterprises which are eligible as collateral for advances to member banks as determined by the Board of Governors of the Federal Reserve System. These include, but are not limited to, debt securities of Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, Federal Farm Credit Bank, and Federal National Mortgage Association. As of December 31, 2011, these investments were rated Aaa, Aa1 and P-1 by Moody's Investors Service and AAA, AA+, and AA by Standard & Poor's Rating Service. As of December 31, 2010, these investments were rated Aaa by Moody's Investors Service and AAA by Standard & Poor's Rating Service.

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DECEMBER 31, 2011 AND 2010**

Note 2 - Cash and Investments (Continued)

As of December 31, 2011, the City's investments in repurchase agreements require a signed and executed 2011 Version of the Global Master Repurchase Agreement, a standardized form published by the Securities Industry and Financial Markets Association ("SIFMA") and International Capital Market Association ("ICMA"), with an approved repo counterparty of the City. Additionally, the City will have to sign and execute a Tri-Party Custodial Agreement between the counterparty and one of the two third-party custodians, JPMorgan Chase and BNY Mellon. The City conducts repo transactions with investment grade rated primary dealers after thorough internal credit due diligence of the counterparty. Securities delivered as collateral must be priced at a minimum of 102% of their market value. Potentially higher margins of 103% to 105% would be used for pricing collateral in a volatile market environment. Parameters for acceptable collateral are determined by the City's investment policy, which abides by Washington State statute. As of December 31, 2011, the securities underlying the City's investments in repurchase agreements have included U.S. Treasuries, U.S. Agency debentures, and U.S. Agency mortgage-backed pass-throughs. The City has not accepted collateral containing credit risk, such as bankers' acceptances, commercial paper, or municipal bonds. Repurchase agreements do not have credit ratings.

Concentration of Credit Risk - The City's investment policy limits concentration of credit risk for the City's investments as a whole, inclusive of the Fund's investments. These policy limits vary for each investment category. The City's investments in which five percent or more is invested in any single issuer, as of December 31, are as follows:

Issuer	2011		2010	
	Fair Value	Percent of Total Investments	Fair Value	Percent of Total Investments
Federal Home Loan Mortgage Corp	\$ 395,358,375	31%	\$ 114,398,437	11%
Federal National Mortgage Association	\$ 317,039,812	25%	\$ 276,373,623	26%
Federal Home Loan Bank	\$ 194,321,359	15%	\$ 218,644,903	21%
Federal Farm Credit Bank	\$ 83,708,078	7%	\$ 100,121,203	9%
Washington State	\$ 68,388,721	5%	\$ -	0%
Wells Fargo	\$ 66,785,435	5%	\$ 32,565,904	3%
Sheffield Receivables Corporation	\$ -	0%	\$ 54,343,164	5%

As of December 31, 2011, the Fund liquidated all dedicated investments to the construction fund account. The Fund's dedicated investments in which five percent or more is invested in any single issuer as of December 31 are as follows:

Issuer	2011		2010	
	Fair Value	Percent of Total Investments	Fair Value	Percent of Total Investments
Federal Home Loan Bank	\$ -	0%	\$ 19,243,813	77%
Federal National Mortgage Association	\$ -	0%	\$ 5,699,375	23%

**SEATTLE PUBLIC UTILITIES -
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Note 3 - Capital Assets

Capital asset activity consisted of the following for the year ended December 31, 2011:

	Beginning Balance	Additions and Transfers In	Retirements and Transfers Out	Ending Balance
Buildings	\$ 14,071,027	\$ 28,702	\$ -	\$ 14,099,729
Structures	133,693,948	16,627,109	- -	150,321,057
Machinery and equipment	582,471,588	36,852,622	(378,605)	618,945,605
Computer systems	46,641,633	2,555,206	(654,710)	48,542,129
Total capital assets, excluding land	776,878,196	56,063,639	(1,033,315)	831,908,520
Less accumulated depreciation	(228,848,784)	(18,332,131)	933,811	(246,247,104)
	548,029,412	37,731,508	(99,504)	585,661,416
Construction in progress	65,071,758	57,742,377	(59,991,708)	62,822,427
Land and land rights	14,279,516	-	-	14,279,516
Other property	662,238	8,721	-	670,959
Capital assets, net	<u>\$ 628,042,924</u>	<u>\$ 95,482,606</u>	<u>\$ (60,091,212)</u>	<u>\$ 663,434,318</u>

Capital asset activity consisted of the following for the year ended December 31, 2010:

	Beginning Balance	Additions and Transfers In	Retirements and Transfers Out	Ending Balance
Buildings	\$ 13,886,080	\$ 184,947	\$ -	\$ 14,071,027
Structures	127,678,398	6,015,550	- -	133,693,948
Machinery and equipment	555,305,459	27,577,447	(411,318)	582,471,588
Computer systems	41,949,377	4,692,256	- -	46,641,633
Total capital assets, excluding land	738,819,314	38,470,200	(411,318)	776,878,196
Less accumulated depreciation	(211,903,507)	(17,279,983)	334,706	(228,848,784)
	526,915,807	21,190,217	(76,612)	548,029,412
Construction in progress	55,054,703	57,269,796	(47,252,741)	65,071,758
Land and land rights	11,090,693	3,188,823	- -	14,279,516
Other property	619,607	42,631	- -	662,238
Capital assets, net	<u>\$ 593,680,810</u>	<u>\$ 81,691,467</u>	<u>\$ (47,329,353)</u>	<u>\$ 628,042,924</u>

During 2011 and 2010, the Fund capitalized interest costs relating to construction of \$3,043,269 and \$2,059,584, respectively.

**SEATTLE PUBLIC UTILITIES -
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Note 4 - Revenue Bonds

The Fund issues bonds to provide financing for capital improvements. Payment of debt service on the bonds is derived solely from the revenues generated by the Fund. The Fund has \$12,777,456 in a debt service reserve fund and has obtained reserve insurance policies to meet the remainder of its reserve requirements. The total bonds outstanding as of December 31, 2011 and 2010 were \$486,610,000 and \$499,785,000, respectively.

Revenue bonds outstanding as of December 31, 2011 and 2010 consisted of the following Municipal Drainage and Wastewater bonds:

Name of Issue	Issuance Date	Maturity Years	Interest Rates	Original Issue Amount	Bonds Outstanding, 2011	Bonds Outstanding, 2010
2001 parity bonds	7/3/01	2002-2031	4.25-5.25%	\$ 60,680,000	\$ 48,880,000	\$ 50,280,000
2002 parity refunding bonds	12/17/02	2003-2032	3.0-5.25%	78,550,000	62,675,000	64,820,000
2004 parity bonds	10/28/04	2005-2034	2.25-5.125%	62,010,000	54,140,000	55,435,000
2006 parity refunding bonds	11/1/06	2008-2037	4.0-5.0%	121,765,000	108,100,000	111,825,000
2008 parity revenue bonds	4/16/08	2009-2038	4.0-5.0%	84,645,000	80,450,000	81,905,000
2009A parity revenue and refunding bonds	12/17/09	2017-2039	4.2-5.5%	102,535,000	102,535,000	102,535,000
2009B parity revenue bonds	12/17/09	2010-2027	2.0-4.0%	36,680,000	29,830,000	32,985,000
				<u>\$ 546,865,000</u>	<u>\$ 486,610,000</u>	<u>\$ 499,785,000</u>

Minimum debt service requirements to maturity on revenue bonds are as follows:

Years Ending December 31,	Principal	Interest	Total
2012	\$ 13,695,000	\$ 23,589,261	\$ 37,284,261
2013	14,290,000	23,042,836	37,332,836
2014	14,935,000	22,455,793	37,390,793
2015	15,590,000	21,847,780	37,437,780
2016	16,340,000	21,177,825	37,517,825
2017 - 2021	92,670,000	93,438,417	186,108,417
2022 - 2026	102,815,000	69,701,717	172,516,717
2027 - 2031	109,000,000	43,217,512	152,217,512
2032 - 2036	75,555,000	18,456,194	94,011,194
2037 - 2041	31,720,000	2,674,433	34,394,433
	<u>\$ 486,610,000</u>	<u>\$ 339,601,768</u>	<u>\$ 826,211,768</u>

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
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DECEMBER 31, 2011 AND 2010**

Note 4 - Revenue Bonds (Continued)

The following table shows the revenue bond activity during the year ended December 31, 2011:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
Revenue bonds	\$ 499,785,000	\$ -	\$ (13,175,000)	\$ 486,610,000	\$ 13,695,000
Add (deduct) deferred amounts:					
Issuance premiums	10,055,705	-	(422,495)	9,633,210	-
Issuance discounts	(1,123,061)	-	45,559	(1,077,502)	-
Loss on refunding	(4,425,742)	-	273,803	(4,151,939)	-
Total bonds payable	<u>\$ 504,291,902</u>	<u>\$ -</u>	<u>\$ (13,278,133)</u>	<u>\$ 491,013,769</u>	<u>\$ 13,695,000</u>

The following table shows the revenue bond activity during the year ended December 31, 2010:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable					
Revenue bonds	\$ 513,070,000	\$ -	\$ (13,285,000)	\$ 499,785,000	\$ 13,175,000
Add (deduct) deferred amounts:					
Issuance premiums	10,478,200	-	(422,495)	10,055,705	-
Issuance discounts	(1,168,620)	-	45,559	(1,123,061)	-
Loss on refunding	(4,699,545)	-	273,803	(4,425,742)	-
Total bonds payable	<u>\$ 517,680,035</u>	<u>\$ -</u>	<u>\$ (13,388,133)</u>	<u>\$ 504,291,902</u>	<u>\$ 13,175,000</u>

Defeasance of Debt - The Fund defeases certain obligations by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. As a result, the old bonds are considered defeased, and the corresponding liabilities and trust account assets are not included in the Balance Sheet. At December 31, 2011 no outstanding bonds are considered defeased. During 2010, \$18,395,000 of 1998 parity bonds was redeemed.

Debt Service Coverage - The revenue bonds contain certain financial covenants, the most significant of which requires the Fund to maintain net revenue available for debt service of at least equal to 125% of average annual debt service. For 2011, net revenue available for debt service, as defined by the bond covenants, was 280% of average annual debt service. For 2010, net revenue available for debt service was 253% of average annual debt service.

**SEATTLE PUBLIC UTILITIES -
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Note 4 - Revenue Bonds (Continued)

Net revenue available for debt service for the years ended December 31, is determined as follows:

	<u>2011</u>	<u>2010</u>
Net operating income	\$ 25,885,634	\$ 19,615,782
Add:		
City taxes	32,448,908	29,177,471
Depreciation and amortization	19,832,129	20,131,347
Investment income	2,820,139	2,595,478
Claims expense	<u>1,515,945</u>	<u>3,728,612</u>
Adjusted net revenue available for debt service	<u>\$ 82,502,755</u>	<u>\$ 75,248,690</u>
Debt service requirement	\$ 29,507,563	\$ 29,774,837
Coverage	280%	253%

Note 5 - Leases

The Fund has non-cancelable operating lease commitments for real and personal property, with payments of \$108,115 and \$105,887 in 2011 and 2010, respectively. Rents are paid as they become due and payable. Minimum lease payments under the leases as of December 31, 2011 are as follows:

2012	\$ 110,248
2013	69,707
2014	59,568
2015	61,610
2016	<u>52,760</u>
	<u>\$ 353,893</u>

Note 6 - Retirement and Other Postemployment Benefit Plans

Pension Costs - All permanent Fund employees are eligible to participate in the Seattle City Employees' Retirement System (the "System"), a cost-sharing public employee retirement system operated by the City. Benefits vest after five years of covered service. City employees may retire after 30 years of service regardless of age; after age 52, with 20 or more years of service; after age 57, with 10 or more years of service, and after age 62, with five or more years of service. The System also provides death and disability benefits. These benefit provisions and all other requirements are established by City ordinances.

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Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

City employees are required to contribute 9.03% of their annual base salaries to the System. The City's contribution rate increased to 9.03% for 2011 from 8.03% in 2009 and 2010. Employer rates are established by the City Council on a biannual basis. The Fund's contributions to the System for the years ended December 31, 2011, 2010 and 2009, were \$3,465,961, \$2,910,580, and \$2,717,853, respectively. The Fund's contribution in 2011 represents its full liability to the System.

The System issues stand-alone financial statements, which may be obtained by writing to the Seattle City Employees' Retirement System, 720 Third Avenue, Suite 900, Seattle, Washington, 98104, telephone: (206) 386-1293.

Employer contributions for the City are as follows (dollars in millions):

<u>Year Ended December 31,</u>	<u>City Required Contribution</u>	<u>City Actual Contribution</u>	<u>Percentage Contributed</u>
2009	\$ 46.7	\$ 46.7	100%
2010	\$ 45.2	\$ 45.2	100%
2011	\$ 50.2	\$ 50.2	100%

Actuarial data and assumptions

Valuation date	January 1, 2011
Actuarial cost method	Entry age
Amortization method	Level percent
Remaining amortization period	30 years, open
Asset valuation method	5-Year Smoothing Method
Investment rate of return	7.75%
Projected general wage inflation	4.0%
Postretirement benefit increases	1.5%

**SEATTLE PUBLIC UTILITIES -
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Schedules of funding progress are as follows (dollars in millions):

Actuarial Valuation Date	Actuarial Accrued						UAAL as a % of Covered Payroll ((b-a)/c)
	Actuarial Value of Assets (a)	Liabilities (AAL) Entry Age ¹ (b)	Unfunded AAL (UAAL) ² (b-a)	Funded Ratio (a/b)	Covered Payroll ³ (c)		
January 1, 2008	\$ 2,119.4	\$ 2,294.6	\$ 175.2	92.4%	\$ 501.9	34.9%	
January 1, 2010	\$ 1,645.3	\$ 2,653.8	\$ 1,008.5	62.0%	\$ 580.9	173.6%	
January 1, 2011	\$ 2,013.7	\$ 2,709.0	\$ 695.4	74.3%	\$ 563.2	123.5%	

- 1 Actuarial present value of benefits less actuarial present value of future normal costs based on entry age actuarial cost method.
- 2 Actuarial accrued liabilities less actuarial value of assets.
- 3 Covered payroll includes compensation paid to all active employees on which contributions are calculated.

Deferred Compensation - The City offers all of its employees a deferred compensation plan (the "Plan") created in accordance with Internal Revenue Code ("IRC") Section 457. The Plan permits employees to defer a portion of their salaries until future years. The deferred compensation is paid to employees upon termination, retirement, death, or unforeseen emergency.

The Plan is an eligible deferred compensation plan under Section 457 of the IRC of 1986, as amended, and a trust exempt from tax under IRC Sections 457(g) and 501(a). The Plan is operated for the exclusive benefit of participants and their beneficiaries. No part of the corpus or income of the Plan shall revert to the City or be used for, or diverted to, purposes other than the exclusive benefit of participants and their beneficiaries. The Plan is not reported in the financial statements of the City or the Fund.

It is the opinion of the City's legal counsel that the City has no liability for investment losses under the Plan. Under the Plan, participants select investments from alternatives offered by the Plan Administrator, who is under contract with the City to manage the Plan. Investment selection by a participant may be changed from time to time. The City does not manage any of the investment selections. By making the selection, participants accept and assume all risks inherent in the Plan and its administration.

Other Postemployment Benefits - Health care plans for active and retired employees are administered by the City as single-employer defined benefit public employee health care plans.

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DECEMBER 31, 2011 AND 2010**

Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Eligible retirees (younger than age 65) may contribute to the medical plan and any additional health care programs contemplated or amended by ordinance of the Seattle City Council and as provided in Seattle Municipal Code 4.50.020.

The Seattle City Council authorizes the obligations of the plan members and the City as employer by passing ordinances and amendments regarding contributions to the plans. Eligible retirees self-pay 100% of the premiums based on blended rates which were established by including the experience of retirees with the experience of active employees for underwriting purposes. The plan is financed on a pay-as-you-go basis, and the City was required to contribute \$3.2 million in 2010 and \$3.0 million in 2009.

The table below summarizes the City's annual cost, expected contributions to the plan, and changes in the net OPEB obligation for fiscal year ended December 31, 2010. These calculations are based on the most recent actuarial valuation data available, dated January 1, 2010. The Fund has accrued \$1,894,828 to the plan as of December 31, 2011, as a reasonable estimate of expected contributions.

	2010	2009
Annual required contribution	\$ 10,709,000	\$ 9,269,000
Interest on net OPEB obligation	898,000	693,000
Adjustment to annual required contribution	<u>(1,239,000)</u>	<u>(915,000)</u>
Annual OPEB cost (expense)	10,368,000	9,047,000
Expected contribution (employer-paid benefits)	<u>(3,202,000)</u>	<u>(2,954,000)</u>
Increase in net OPEB obligation	7,166,000	6,093,000
Net OPEB obligation, beginning of year	<u>20,446,000</u>	<u>14,353,000</u>
Net OPEB obligation, end of year	<u>\$ 27,612,000</u>	<u>\$ 20,446,000</u>
Fund's allocated share of city liability	<u>\$ 1,378,711</u>	<u>\$ 973,362</u>

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially-determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. Actuarial calculations are based on the types of benefits provided under the terms of the plan and on the pattern of shared costs between the employer and plan members, at the time of each valuation. The projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost sharing between the employer and plan members in the future. Actuarial calculations reflect a long-term perspective. Consistent with that perspective, actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

**SEATTLE PUBLIC UTILITIES -
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Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Significant methods and assumptions are as follows:

Actuarial data and assumptions

Valuation date	January 1, 2010
Actuarial cost method	Entry age normal
Amortization method	Level dollar
Remaining amortization period	30 years, open
Discount rate	4.39%
Health care cost trend rates - medical	10.0%, decreasing by 0.5% for each year for 10 years to an ultimate rate of 5%.
Participation	40% of Active Employees who retire participate.
Mortality	General Service Actives and Retirees based on the Group Annuity Mortality (GAM) 1994 Static Table (Final) with ages set forward one year.
Marital status	60% of members electing coverage are assumed to be married or to have a registered domestic partner. Male spouses two years older than their female spouses.
Morbidity factors	Morbidity rate ranges for ages 50 through 64: 104.25% to 203.61% for male retirees, 76.78% to 149.96% for female retirees, 123.03% to 229.84% for male spouses, and 90.62% to 169.29% for female spouses. Retirees' spouses pay a lower premium than retirees.
Other considerations	Active employees with current spousal and/or dependent coverage are assumed to elect same plan and coverage after retirement.

**SEATTLE PUBLIC UTILITIES -
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Note 6 - Retirement and Other Postemployment Benefit Plans (Continued)

Schedules of funding progress are as follows (dollars in millions):

Actuarial Valuation Date	Actuarial Value of Assets (a)	AAL Entry Age (b)	UAAL (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percent of Covered Payroll ((b-a)/c)
January 1, 2008	\$ -	\$ 78.8	\$ 78.8	0.0%	NA	NA
January 1, 2009	\$ -	\$ 84.1	\$ 84.1	0.0%	NA	NA
January 1, 2010	\$ -	\$ 93.5	\$ 93.5	0.0%	NA	NA

The Health Care Subfund of the General Fund is reported in the City's Comprehensive Annual Financial Report which can be obtained by writing the Department of Finance, City of Seattle, PO Box 94747, Seattle, WA 98124-4747.

Note 7 - Claims Payable

The City and the Fund are self-insured for certain losses arising from personal and property damage claims by third parties and for casualty losses to the Fund's property. Liabilities for identified claims and claims incurred but not reported have been recorded by the Fund.

For 2011 and 2010, liabilities for workers' compensation claims, as well as other claims, are discounted over a 15-year period at the City's rate of return on investments, 0.824% and 1.027%, respectively. Claims expected to be paid within one year were \$3,459,286 and \$3,468,383 as of December 31, 2011 and 2010, respectively. The schedules below present the changes in the liability for workers' compensation claims and other claims (risk financing liabilities) as of December 31:

	2011	2010
Beginning liability, undiscounted	\$ 13,011,297	\$ 12,063,426
Payments	<u>(1,827,970)</u>	<u>(2,827,768)</u>
Incurred claims and change in estimate	<u>1,422,624</u>	<u>3,775,639</u>
Ending liability, undiscounted	<u><u>\$ 12,605,951</u></u>	<u><u>\$ 13,011,297</u></u>
Ending liability, discounted (recorded balance at December 31)	<u><u>\$ 12,289,809</u></u>	<u><u>\$ 12,601,834</u></u>

The Fund is involved in litigation from time to time as a result of operations. Claims are pursued if determined to be in the best interest of the Fund's customers.

**SEATTLE PUBLIC UTILITIES -
DRAINAGE AND WASTEWATER FUND
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Note 8 - Compensated Absences

The Fund has recorded a liability for earned but unused holiday, compensatory, merit, and vacation leave, as well as estimated sick leave payments calculated based on the termination payment method. The schedules below show the compensated absences activity during the years ended December 31, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Beginning liability	\$ 4,282,579	\$ 3,824,275
Additions	3,475,788	4,764,200
Reductions	<u>(3,333,413)</u>	<u>(4,305,896)</u>
Ending liability	<u>\$ 4,424,954</u>	<u>\$ 4,282,579</u>

Note 9 - Environmental Liabilities

Following is a brief description of the significant sites that require environmental remediation:

Duwamish Sites - The U.S. Environmental Protection Agency ("EPA") has indicated that it will require the clean-up and remediation of certain Duwamish sites under its Superfund authority. No specific requirements for remediation by potentially responsible parties ("PRP") have been made by the EPA as of the date of this report, except related to specific "early action sites" which are or have been under Administrative Orders on Consent ("AOC"). In order to manage the liability, the City is working with the EPA and other PRP's on a Remedial Investigation ("RI") and Feasibility Study ("FS") to evaluate the risk to human health and the environment within the six mile superfund area, identify the possible early action clean-up sites, and generally evaluate the feasibility of clean-up options for use in the ultimate remedial actions that the EPA will require. The Remedial Investigation document has been completed and the draft Feasibility Study was submitted to the EPA at the end of 2010. The EPA will likely complete their proposed plan in 2012 followed by a Record of Decision in 2013.

The Fund, together with other PRP's, has voluntarily agreed to initiate clean-up of two early action sites identified during the RI under EPA issued Administrative Orders on Consent: Slip 4 and T-117.

East Waterway Site - In 2006 the EPA issued an AOC for a Supplemental RI and FS for the East Waterway, an operable unit of the Harbor Island Superfund Site. Subsequent to an agreement between the EPA, the Port of Seattle ("Port"), King County and the City, the Port alone signed the order. Both the City and King County signed a Memorandum of Agreement with the Port to participate as cost share partners in the work required by the EPA. No specific requirements for remediation by PRPs have been made by the EPA as of the date of this report. The Remedial Investigation is anticipated to be completed by 2014.

**SEATTLE PUBLIC UTILITIES -
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NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2011 AND 2010**

Note 9 - Environmental Liabilities (Continued)

Gas Works Park Sediment Site - In April 2002, the Department of Ecology ("DOE") named the City and another party, Puget Sound Energy, as PRPs for contamination at the Gas Works Sediments Site in North Lake Union. The City and Puget Sound Energy signed an Agreed Order with the DOE in 2005 to initiate two RI and FSs for the sediment site - one in the western portion of the site led by the City, and another in the eastern portion of the site led by Puget Sound Energy. The City, with the Fund as lead, is now working to complete the RI and FS for the western portion of the site for submittal to the DOE. The RI and FS include an evaluation of the nature and extent of contamination on the site, an evaluation of multiple alternatives for remediating the sediments and a recommended preferred alternative. Recently the EPA has begun in-depth discussions with DOE. As a result, a Clean-up Action Plan is expected from the Department of Ecology in 2015 or 2016.

North Boeing Field/Georgetown Steam Plant - The City, King County and Boeing have signed an Administrative Order with the DOE requiring them to investigate and possibly remove contamination in an area that encompasses North Boeing Field, the Georgetown Steam Plant, and the King County Airport.

7th Avenue South Pump Station - The City acquired land in the South Park area of Seattle to construct the 7th Ave South Pump Station. The land was determined to be contaminated subsequent to the purchase. The Fund has voluntarily agreed to clean up the contamination in order to continue with the planned construction of the pump station. The cleanup is anticipated to be completed in 2012.

The Fund has included in its estimated liability those portions of the environmental remediation work that are currently deemed to be reasonably estimable. Cost estimates were developed using the expected cash flow technique in accordance with GASB 49. Estimated outlays were based on current cost and no adjustments were made for discounting or inflation. Cost scenarios were developed for a given site based on data available at the time of estimation and will be adjusted for changes in circumstance. Scenarios consider the relevant potential requirements and are adjusted when benchmarks are met or when new information revises estimated outlays, such as changes in the remediation plan or operating conditions. Costs were calculated on a weighted average that was based on the probabilities of each scenario being selected and reflected cost-sharing agreements in effect. In addition, certain estimates were derived from independent engineers and consultants. The estimates were made with the latest information available; however, as new information becomes available, estimates may vary significantly due to price fluctuations, technological advances, or applicable laws or regulations.

The Fund is aggressively pursuing other third parties that may have contributed to the contamination of the sites noted. The Fund's estimate for not yet realized recoveries from other parties for their share of remediation work that offset the Fund's estimated environmental liability was \$6.3 million and \$4.9 million, as of December 31, 2011 and 2010, respectively. During 2010, the Fund received an environmental cost recovery of \$2.4 million from Boeing. The recovery represented settlement for prior legal costs incurred in defining their cost share in remediating the contaminated sites in the future. No cost recovery funds were received in 2011.

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Note 9 - Environmental Liabilities (Continued)

The following changes in the provision for environmental liabilities at December 31 are:

	<u>2011</u>	<u>2010</u>
Beginning environmental liability, net of recovery	\$ 10,599,933	\$ 10,243,773
Payments or amortization	(2,848,308)	(2,794,071)
Incurred environmental liability	<u>804,200</u>	<u>3,150,231</u>
Ending environmental liability, net of recovery	<u><u>\$ 8,555,825</u></u>	<u><u>\$ 10,599,933</u></u>

The provision for environmental liabilities included in current and non-current liabilities at December 31 are:

	<u>2011</u>	<u>2010</u>
Environmental liability, current	\$ 2,263,979	\$ 2,839,874
Environmental liability, noncurrent	<u>6,291,846</u>	<u>7,760,059</u>
Ending liability	<u><u>\$ 8,555,825</u></u>	<u><u>\$ 10,599,933</u></u>

Note 10 - Public Works Trust and Other Loans

The Fund has various construction projects that are financed by low interest loans issued by the State of Washington. The loan agreements require that the Fund finance a portion of these projects from other sources. These loans have been used to enhance the drainage system. The fund also financed the purchase of land with a small loan in the amount of \$161,000 from a private party.

In 2011, the Fund was approved for a public works trust fund loan of \$3,574,418 from the Washington State Department of Commerce for construction and site improvements in the Midvale area of Seattle. Amounts borrowed under this agreement accrue interest at 0.5% per annum and are to be repaid by June 2032.

In 2010, the Fund made an additional draw on a loan in the amount of \$170,000 from the Washington State Department of Commerce for construction and site improvements in the South Park Area. Amounts borrowed under this agreement accrue interest at 0.5% per annum and are to be repaid by June 2025.

The Fund was approved for a public works trust fund loan in 2009 in the amount of \$1,394,678 from the Washington State Department of Ecology. This loan is funded with resources from the American Recovery and Reinvestment Act of 2009 (ARRA), which provides a 50% forgivable provision. In 2010, the Fund borrowed \$718,726 of which \$359,363 is forgivable. More draw downs are expected in the future.

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Note 10 - Public Works Trust and Other Loans (Continued)

Loans outstanding as of December 31, 2011 and 2010 are as follows:

Description	Maturity Years	Interest Rate	Amount Borrowed	Loans Outstanding 2011	Loans Outstanding 2010
Private Loan	1999-2013	7.0%	\$ 161,100	\$ 26,134	\$ 40,956
Midvale	2013-2032	0.50%	4,000,000	3,574,418	-
Thornton Creek Natural Drainage Systems	2004-2024	0.50%	3,700,000	2,546,471	2,742,352
High Point Natural Drainage Systems	2010-2029	1.50%	2,679,413	2,421,364	2,541,470
South Park Flood Control and Local Drainage Program	2005-2025	0.50%	3,400,000	2,759,719	2,956,842
Ballard Green Streets ARRA Project	2013-2022	2.90%	359,363	572,558	359,363
Thornton Creek Water Quality Project	2009-2030	1.50%	6,983,021	6,697,098	6,983,021
			<u>\$ 21,282,897</u>	<u>\$ 18,597,762</u>	<u>\$ 15,624,004</u>

Minimum debt service requirements to maturity on long term loans are as follows:

Years Ending December 31,	Principal	Interest	Total
2012	\$ 903,774	\$ 180,218	\$ 1,083,992
2013	906,474	196,215	1,102,689
2014	1,092,756	175,618	1,268,374
2015	1,101,338	164,130	1,265,468
2016	1,110,076	152,487	1,262,563
2017-2021	5,613,748	582,684	6,196,432
2022-2026	4,941,434	303,266	5,244,700
2027-2031	2,928,162	71,362	2,999,524
	<u>\$ 18,597,762</u>	<u>\$ 1,825,980</u>	<u>\$ 20,423,742</u>

The following table shows the loan activity during the years ended December 31:

	2011	2010
Net public works trust loans, beginning of year	\$ 15,624,004	\$ 13,310,901
Loan proceeds	3,818,263	2,846,570
Principal payments	<u>(844,505)</u>	<u>(533,467)</u>
Net public works trust loans, end of year	<u>\$ 18,597,762</u>	<u>\$ 15,624,004</u>
Public works trust loans due within one year	\$ 903,774	\$ 814,130
Public works trust loans, noncurrent	<u>\$ 17,693,988</u>	<u>\$ 14,809,874</u>

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Note 11 - Notes and Contracts Receivable

The Fund has an agreement with the Seattle Housing Authority for the recovery of the remaining unreimbursed cost of the Fund's contributions of public infrastructure to the New Holly redevelopment project. As of December 31, 2011 the Seattle Housing Authority receivable was \$1,341,705, which will be repaid over 30 years.

In April 2011, the Fund entered into an agreement with private individuals for a sewer connection charge contract. The receivable was \$9,309 at year end 2011.

Notes and contracts receivable are composed of the following as of December 31:

	2011	2010
Seattle Housing Authority receivable	\$ 1,341,705	\$ -
Dalcerro receivable	9,309	-
Total notes and contracts receivable	1,351,014	-
Due within one year	(44,690)	-
Total non-current notes and contracts receivable	<u>\$ 1,306,324</u>	<u>\$ -</u>

Note 12 - Wastewater Disposal Agreement

The Fund has a wastewater disposal agreement with the King County Department of Natural Resources Wastewater Treatment Division (the "Division"), which expires in 2036. The monthly wastewater disposal charge paid to the Division is based on the Division's budgeted cost for providing the service. The charges are determined by water consumption and the number of single-family residences as reported by SPU and other component agencies. Payments made by the Fund were \$123,702,566 and \$110,799,772 for fiscal years 2011 and 2010, respectively.

SUPPLEMENTAL INFORMATION

**SEATTLE PUBLIC UTILITIES -
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SUPPLEMENTAL INFORMATION**

Statistics Required for Revenue Bond Continuing Disclosure

Wastewater System Operating Statistics

	2007	2008	2009	2010	2011
Population Served	586,200	592,800	602,000	612,000	612,100
Billed Wastewater Revenues	\$ 160,917	\$ 164,837	\$ 185,058	\$ 185,473	\$ 202,885
Billed Wastewater Volume (MG)					
Residential	6,027	5,931	5,941	5,870	5,535
Commercial	<u>10,196</u>	<u>9,988</u>	<u>9,834</u>	<u>9,752</u>	<u>9,577</u>
Total	<u>16,223</u>	<u>15,919</u>	<u>15,775</u>	<u>15,622</u>	<u>15,112</u>
Gallons Used per Day per Capita	75.8	73.6	71.8	69.9	67.6

Drainage and Wastewater - 2011 Accounts and Billed Revenues

Customer Accounts	Drainage	Wastewater
Residential	139,018	164,276
Commercial	<u>73,555</u>	<u>20,654</u>
Total	<u>212,573</u>	<u>184,930</u>
Billed Revenue	Drainage	Wastewater
Residential	\$ 33,171,813	\$ 73,963,652
Commercial	<u>35,265,351</u>	<u>128,921,800</u>
Total	<u>\$ 68,437,164</u>	<u>\$ 202,885,452</u>

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Major Wastewater Customers - 2011 Annual Billed Revenues and Volumes

Name	Revenue	Volume
University of Washington	\$ 5,797,527	674,151
Seattle Housing Authority	\$ 2,444,775	241,010
City of Seattle	\$ 1,864,321	187,204
King County	\$ 1,257,366	125,176
Port of Seattle	\$ 951,655	121,417
Darigold	\$ 869,700	74,210
Harborview Medical Center	\$ 788,913	82,349
Swedish Medical Center	\$ 762,378	89,220
Virginia Mason	\$ 713,909	72,062
Boeing Commercial Airplane Group	\$ 700,370	68,020

Major Drainage Customers - 2011 Annual Billed Revenues and Acreage

Name	Revenue	Acres
City of Seattle	\$ 4,549,371	5,143
Port of Seattle	\$ 2,682,237	967
Seattle Public Schools	\$ 1,311,587	685
King County	\$ 1,172,259	571
BNSF Rwy Co.	\$ 980,943	417
University of Washington	\$ 965,814	568
United States Government	\$ 616,129	300
Seattle Housing Authority	\$ 575,350	337
Union Pacific Railroad Co.	\$ 405,018	154
Seattle Community Colleges	\$ 258,395	158

**SEATTLE PUBLIC UTILITIES -
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Wastewater Rates

	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
Volume rate per ccf	\$7.45	\$7.75	\$8.89	\$8.98	\$10.28	\$10.68

Note: 1 CCF equals 748 gallons. Wastewater rate increased 14.5% and 1.0% in 2011 and 2010, respectively.

Drainage Rates

Flat Rate per Parcel						% Impervious Space
	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	
Single Family Residential*						
< 3,000 sq. ft.	\$ 91.38	\$ 102.90	\$ 104.90	\$ 134.06	\$ 149.33	
3,000 - 4,999 sq. ft.	\$ 132.65	\$ 149.56	\$ 152.46	\$ 173.10	\$ 192.79	
5,000 - 6,999 sq. ft.	\$ 179.27	\$ 202.17	\$ 206.09	\$ 234.94	\$ 261.66	
7,000 - 9,999 sq. ft.	\$ 213.00	\$ 256.38	\$ 261.35	\$ 298.32	\$ 332.23	
Rate per 1,000 sq. ft.						
Undeveloped						
Regular	\$ 11.21	\$ 16.85	\$ 17.18	\$ 19.72	\$ 21.96	0 - 15%
Low Impact	\$ 9.09	\$ 10.19	\$ 10.39	\$ 12.35	\$ 13.76	
Light						
Regular	\$ 18.58	\$ 25.20	\$ 25.69	\$ 29.62	\$ 32.98	16 - 35%
Low Impact	\$ 16.99	\$ 18.98	\$ 19.35	\$ 23.47	\$ 24.14	
Medium						
Regular	\$ 32.83	\$ 36.61	\$ 37.32	\$ 42.89	\$ 47.76	36 - 65%
Low Impact	\$ 26.63	\$ 29.70	\$ 30.28	\$ 34.43	\$ 38.35	
High	\$ 42.52	\$ 47.34	\$ 48.26	\$ 56.57	\$ 63.01	66 - 85%
Very High	\$ 50.53	\$ 56.23	\$ 57.32	\$ 66.90	\$ 74.49	86 - 100%

* Prior to 2008, all single family residential (SFR) parcels were billed a flat rate per parcel. Since 2008, SFR parcels less than 10,000 sq. ft. have been billed a flat rate that depends on parcel size. Larger SFT parcels have been billed under the commercial rate structure.