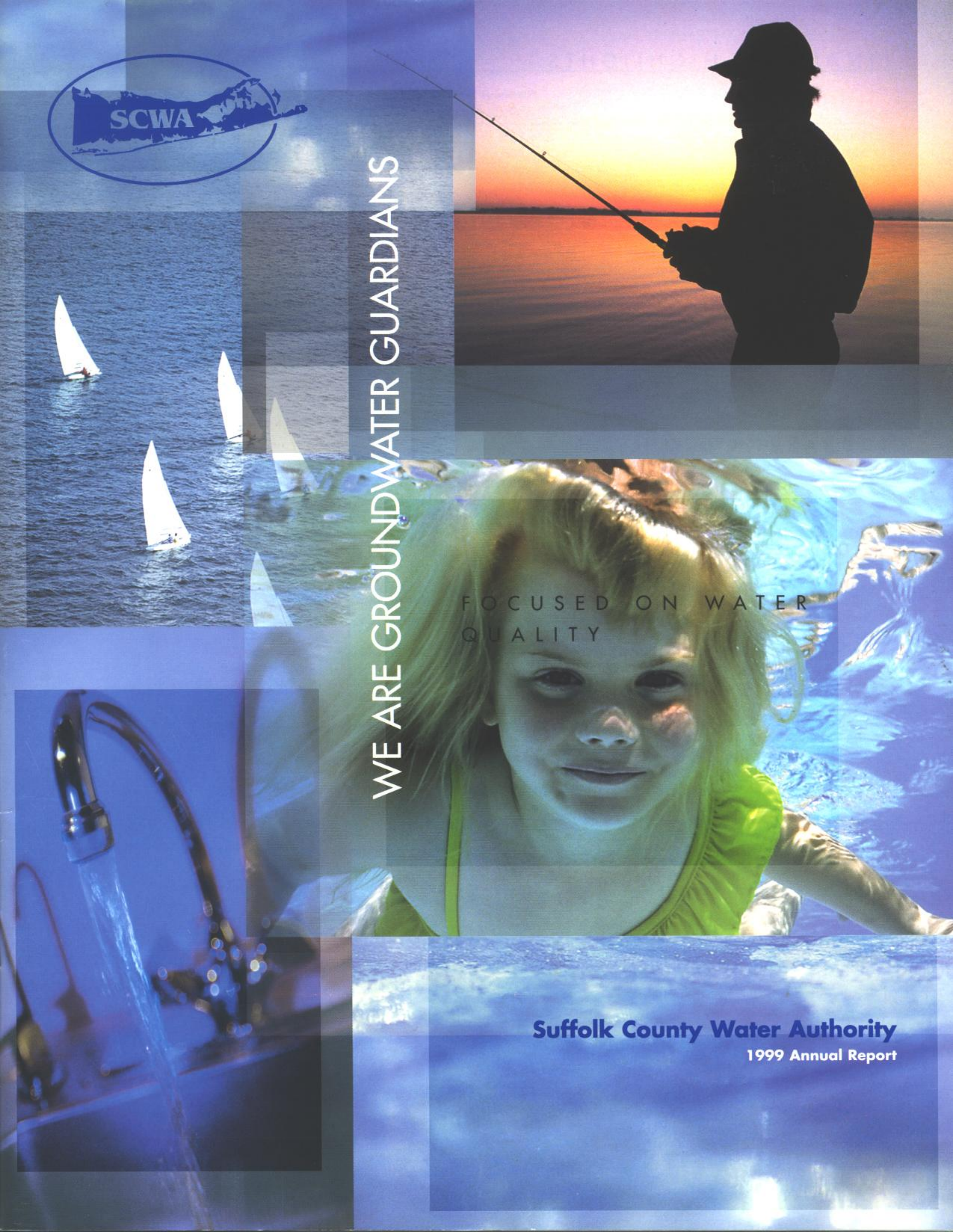


WE ARE GROUNDWATER GUARDIANS

FOCUSED ON WATER QUALITY

Suffolk County Water Authority

1999 Annual Report

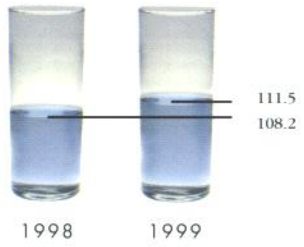
FINANCIAL HIGHLIGHTS

	For Fiscal Year Ended May 31 1999	1990	10-Year Growth	Percent Increase
Customers	**334,754**	291,550	43,204	15%
Miles of Main	**5,023**	4,235	788	19%
Fire Hydrants	**30,865**	26,468	4,397	17%
Water Pumped (Billion Gallons)	**62,184**	43,361	18,823	43%
Employees	**577**	588	(11)	(2)%
Gross Revenues	**$111,424,000**	$ 63,861,000	$ 47,563,000	74%
Operating and Maintenance Expense	**55,043,000**	40,507,000	14,536,000	36%
Water Plant at Cost	**863,144,000**	477,209,000	385,935,000	81%
Bonded Indebtedness	**337,114,000**	146,455,000	190,659,000	130%
Total Cumulative Earnings	**205,890,000**	134,796,000	71,094,000	53%

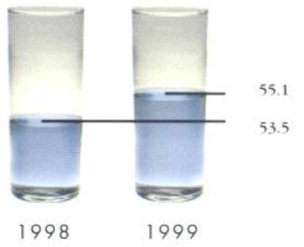
1998–1999 HIGHLIGHTS

	May 31, 1999	May 31, 1998
Total Revenues	**$111,424,000**	$108,189,000
Operating and Maintenance Expense Except Depreciation	**55,043,000**	53,547,000
Interest on Bonds and Notes; Including Amortization of Debt Discount and Expense	**19,653,000**	20,786,000
Depreciation	**15,315,000**	13,950,000
Revenues Invested in Facilities for the Year	**20,582,000**	17,696,000
Revenues Invested in Facilities (since June 1, 1951)	**205,890,000**	185,308,000
Total Water Plant at Cost	**863,144,000**	808,790,000
Net Additions to Water Plant	**56,132,000**	55,764,000
Customers (Active Services)	**334,754**	331,041
Miles of Main in Service	**5,023**	4,905
Fire Hydrants in Service	**30,865**	30,275
Water Production (Billion Gallons)	**62.1**	58.4

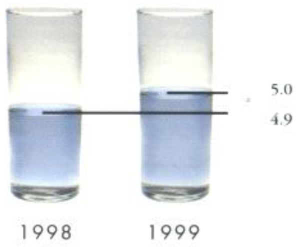
REVENUES
(dollars in millions)



EXPENSES
(dollars in millions)



MILES OF MAIN
(miles in thousands)



AUTHORITY PROFILE

The SCWA is a self-supporting, public benefit corporation operating by virtue of the Public Authorities Law of the State of New York. It is without taxing power and operates as a business enterprise. The Authority is neither an agency of New York State nor Suffolk County Government.

The only revenue the Authority receives is that obtained from the sale of water to its customers. The Authority is non-profit; all revenue received must be used for operating expenses, construction costs, and for paying outstanding debts.

The Suffolk County Water Authority is the largest groundwater supplier in the nation and has been operating for 48 years. Currently, the SCWA serves more than one million Suffolk County residents. The Authority is operated solely for the benefit of the customers it serves.

AUTHORITY MEMBERS *(from left to right)*:
James T.B. Tripp, Esq., John E. Gee, Jr.,
Michael A. LoGrande, Eric J. Russo, Esq.,
Melvin M. Fritz, D.O., M.D.

Most of the wells used by the Suffolk County Water Authority—which operates the largest water system in the nation based entirely on groundwater—draw from the Upper Glacial and Magothy aquifers. The deepest aquifer beneath Suffolk County, the Lloyd, remains largely untapped and holds tremendous amounts of water, much of which has been stored there for thousands of years.

CHAIRMAN'S MESSAGE

If it stopped raining on Long Island today and the population and water use remained constant, residents of Suffolk and Nassau Counties would have more than enough water to drink, bathe, wash their clothes and cars and water their lawns for the next 500 years.

Quantity, however, is not enough if the quality of that water is allowed to deteriorate. Without vigilant stewardship, that enormous water supply could come to remind us of the Ancient Mariner's sorrowful lament: "Water, water everywhere, nor any drop to drink."

The Suffolk County Water Authority has vowed to provide that vigilant stewardship. Its record over the years shows that it continues to carry out its responsibility, providing nearly 1.2 million people with the best possible water at the lowest possible price.

Since 1999 marks a decade of my leadership, and also coincides with the end of this century, it seems appropriate that I review the past as a prelude to facing the challenges of the future. Our many accomplishments this past year include achieving full Y2K compliance and mailing the most comprehensive Annual Water Quality Statement the SCWA has ever produced for its customers.

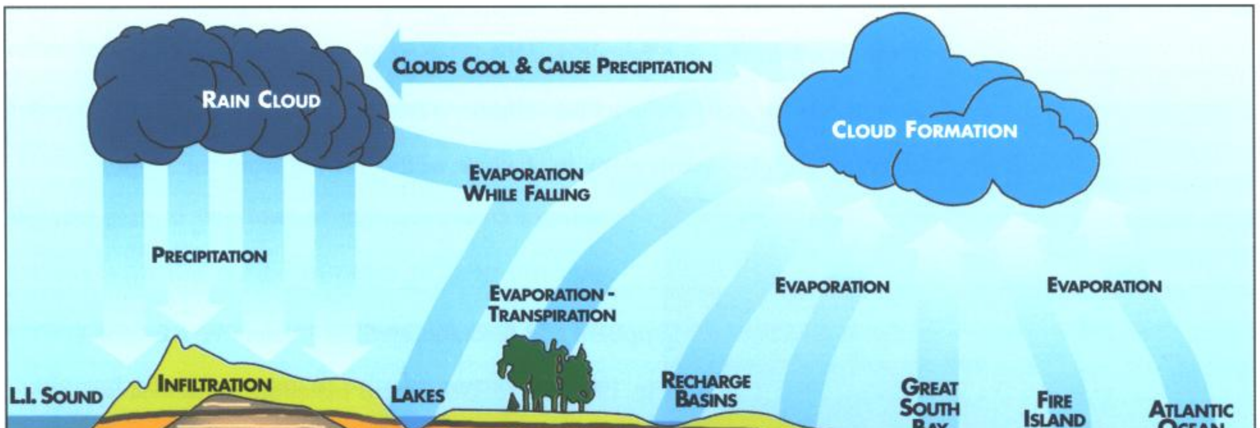
But let me start at the beginning. Long Island has the largest entirely underground water system in the United States. Any true understanding of that system must take us back tens of thousands of years, when advancing and retreating glaciers piled up alternating layers of sand and thick clay. The hardy, impervious clay layers began to serve as filters, protecting the gathering waters in deep aquifers. This natural phenomenon is unique in the United States because, not only are the sand deposits thick enough to hold enormous amounts of water between the sand particles, but the sand and clay layers filter the precipitation that falls on land surfaces above, constantly recharging the aquifers below.

Most of our drinking water comes from the top two layers of Pleistocene Epoch deposits, the Upper Glacial and Magothy aquifers. The clay between them is called the Gardiner Clays. Below the Magothy lies another clay layer, the Raritan Clays, and beneath the Raritan is another sand and gravel aquifer referred to as the Lloyd. While Nassau, on the west, has many Lloyd wells, Suffolk had only four out of a total of 426 active wells up to the 1998/1999 fiscal year. This leaves Suffolk with a considerable reserve of water with one exception—the East End. The Towns of Southold, Shelter Island, and East Hampton (Montauk area) have limited aquifers beneath them which are layers saturated with saltwater. The cost to move the larger reserves easterly is prohibitive.

Initial U.S. Geological Survey estimates set the volume of water stored in the Upper Glacial and Magothy layers on Long Island at approximately 60 trillion gallons. Some estimates even suggest all three aquifers contain more than 100 trillion gallons. The amount pumped by all water suppliers and private wells on Long Island is about 120 billion gallons a year. And, of course, rains and melting snow constantly replenish the water supply. In normal years, the amount of water absorbed in the aquifers far exceeds the amount removed through pumpage. This is evidenced by the continual flowing rivers that serve as aquifer relief valves.

Quality considerations, however, are a different matter. Advances in organic chemistry and increased population are two of the major factors that have rendered this very critical aspect of our mandate increasingly difficult to address. To speak of *advances* in organic chemistry may be a misnomer. Diverse chemical products have been introduced in recent decades including fuel additives, detergents, degreasers, pesticides, herbicides, fungicides, insecticides and concentrated fertilizers. While these products were developed to make life easier or better, their residual effects on groundwater were found to have an impact on human health. As more studies were done, many new and more stringent safety levels were established for these contaminants.

Such research has determined that the quality of our groundwater is also threatened by all sorts of chemicals that modern families use every day. For example, it is estimated that the average adult uses nearly 100 chemical compounds while getting ready for work in the morning. A simple reading of labels on toothpaste, hair sprays, deodorants, soap, shaving cream, after shave, shampoo, and conditioners would reveal a great many chemical compounds that can eventually find their way into groundwater.



Another danger to the water supply comes from septic waste. Approximately 15 percent of Suffolk homes are served by sanitary sewer systems. The remaining 85 percent deposit their septic waste directly into cesspools that leach into the ground. While cesspools provide some anaerobic decontamination, or primary treatment of wastewater, some of the waste components filter through the sand layers, resulting in additional contamination.

As Suffolk's population has doubled over the last 40 years—from 600,000 to 1.4 million—other sources of contamination have grown along with it. For example, there has been an increase in the number of oil tanks buried in our county, and many have begun to leak. Improper disposal methods for contaminants like engine waste oil and freon add to the pollution of the soil and, ultimately, the water supply—particularly in shallow wells drawing from the Upper Glacial aquifer.

Stricter health laws enacted years ago required that water suppliers add filtration systems to remove harmful chemicals, to ensure that tap water would be safe to drink. In 1989, the SCWA began installing 30 activated carbon filter systems at a cost of nearly $1 million dollars each. Not every well requires a filter, and we have continued to maintain and install carbon filters as needed, resulting in virtually pure water with modest cost increases to our customers. During the 1998/1999 fiscal year, nearly 45 percent of our wells had carbon filters.

While higher government standards are being enacted to protect the public, the standards in New York State continue to be the most stringent in the nation. In addition, the SCWA has imposed even stricter standards on itself. During the 1998/1999 fiscal year, our state-of-the-art laboratory tested for more than 200 different contaminants in over 60,000 samples—and still managed to receive a perfect score on the required proficiency test administered by the New York State Department of Health.

Most SCWA wells reach the deeper layers, where water quality is good to excellent. Private wells, however, are generally shallow—from 50 to 150 feet in depth. Consequently, private wells are far more vulnerable to surface contaminants. Families with private wells are not required to test them, and may do so infrequently or not at all. During the 1998/1999 fiscal year, the Suffolk County Department of Health Services continued to encourage those still dependent on the approximately 65,000 private wells in Suffolk County to convert to public water where possible. This, too, is a trend we expect to see extended into the future. It is very likely that most of these existing wells will be replaced by SCWA water over the next 15 years.

We also plan to continue to improve our communications with the public in order to help our customers have a better understanding of what we are doing and what they can do to manage and protect their water supply. During fiscal year 1998/1999, we dramatically improved our quarterly bill inserts, enhanced the SCWA website, and continued to support the Volunteer Environmental Educators Program (VEEP) run by the Suffolk County Department of Health Services. Similarly, our efforts to become certified by the national Groundwater Foundation as a Groundwater Guardian

A turning point in the management of our water resources was reached during this century's final decade when the Suffolk County Water Authority took the initiative to help create the landmark Pine Barrens Law. Because we were able to bring environmentalists and developers together to design a practical, detailed plan to protect critical watershed areas, Long Island's largest preservation program ever is now firmly established.

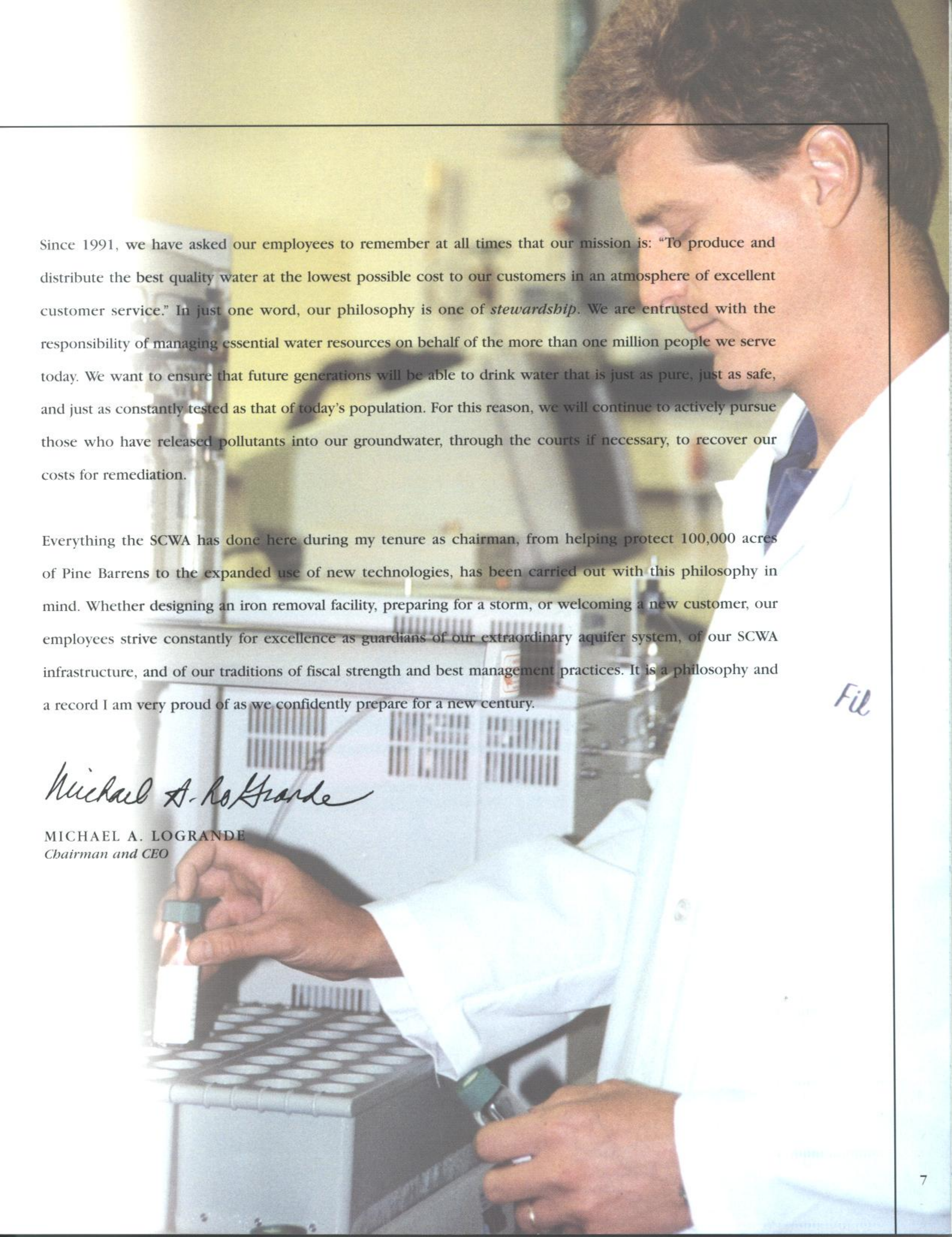
Although iron is naturally present in water and does not pose a health hazard, the Suffolk County Water Authority's "Rustbusters" work diligently to improve the aesthetic appeal of our product. Our engineers designed the standardized iron removal unit shown below based on SCWA's experience with its first iron removal plant, which opened on Harvest Lane in West Islip in 1996. During the 1998/1999 fiscal year, we brought three new plants on line while designing and constructing six scheduled plants that will begin operating during the fiscal year ending May 31, 2000.

Community came to fruition during the fall of 1998, and our participation in this program will continue.

Behind the scenes, the decade of the 1990s has been one of increased productivity and professionalism on the part of our staff. Our employees are highly qualified, provided with state-of-the-art technology, and expected to uphold the highest ethical standards.

During the 1998/1999 fiscal year, as in the previous 48 years of our history, our engineers and technicians exercised the highest professional standards as they maintained our system. They decided which elements of the aging infrastructure needed to be replaced, when introducing new technology would benefit our customers, and where, if feasible, to expand our system in response to the requests we constantly receive. We welcomed approximately 3,700 new customers during the past fiscal year, and we added nearly 120 miles of main. We will continue to uphold these standards as we move forward.

Over the next few decades, the SCWA will expand its infrastructure replacement program for those parts of our system that are beginning to show signs of stress due to aging. These programs will provide substantial improvement to water quality and pressures while reducing service interruptions due to main breaks.



Since 1991, we have asked our employees to remember at all times that our mission is: "To produce and distribute the best quality water at the lowest possible cost to our customers in an atmosphere of excellent customer service." In just one word, our philosophy is one of *stewardship*. We are entrusted with the responsibility of managing essential water resources on behalf of the more than one million people we serve today. We want to ensure that future generations will be able to drink water that is just as pure, just as safe, and just as constantly tested as that of today's population. For this reason, we will continue to actively pursue those who have released pollutants into our groundwater, through the courts if necessary, to recover our costs for remediation.

Everything the SCWA has done here during my tenure as chairman, from helping protect 100,000 acres of Pine Barrens to the expanded use of new technologies, has been carried out with this philosophy in mind. Whether designing an iron removal facility, preparing for a storm, or welcoming a new customer, our employees strive constantly for excellence as guardians of our extraordinary aquifer system, of our SCWA infrastructure, and of our traditions of fiscal strength and best management practices. It is a philosophy and a record I am very proud of as we confidently prepare for a new century.

Michael A. LoGrande

MICHAEL A. LOGRANDE
Chairman and CEO

AUTHORITY MEMBERS

Michael A. LoGrande
Chairman/Chief Executive Officer

Melvin M. Fritz, D.O., M.D.
Secretary

John E. Gee, Jr.

Eric J. Russo, Esq.

James T.B. Tripp, Esq.

MANAGEMENT STAFF

Michael A. LoGrande
Chairman/Chief Executive Officer

Frank Faber
Chief Financial Officer

Robert G. Graven
Deputy Chief Executive Officer for Customer Service

Herman J. Miller
Deputy Chief Executive Officer for Operations

Michael Stevenson
Deputy Chief Executive Officer for Administration

William C. Arabio
Director of Information Services

Robert L. Murray
Director of Production Control

Joseph M. Pokorny
Chief Engineer

Karen Randazzo
Director of Laboratory Services

Donald Slotnick
Director of Distribution

Andrew Varanelli
Director of General Services

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Counsel

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Bond Trustee

PricewaterhouseCoopers LLP
Independent Accountants

Smith Barney Harris Upham & Co., Inc.
Financial Consultant

Leggette, Brashears & Graham, Inc.
Consulting Groundwater Geologists

FINANCIAL SECTION

BALANCE SHEET

(Amounts in thousands)

	May 31, 1999	1998
ASSETS		
Water plant, at cost less accumulated depreciation	$688,189	$646,445
Current assets		
Cash and cash equivalents	5,530	39,569
Short-term investments	31,793	7,227
Accounts receivable, less allowance for doubtful accounts of $700 in 1999 and $675 in 1998	8,887	9,393
Accrued water services and fire protection revenues	12,686	10,857
Interest and other receivables	756	2,956
Materials and supplies, at average cost	5,152	5,239
Prepayments and other current assets	1,048	954
Total current assets	65,852	76,195
Funds held by fiscal agent	18,155	18,168
Long-term investments	32,065	18,786
Construction fund	27,680	65,229
Intangible assets	7,964	8,779
Other assets	5,467	7,329
	91,331	118,291
	$845,372	$840,931
CAPITALIZATION AND LIABILITIES		
Capitalization		
Water System Revenue Bonds, less current portion and unamortized discount	$326,001	$324,498
Bond anticipation notes payable	76,600	81,400
Contributions in aid of construction	184,579	175,383
Revenue invested in facilities	205,890	185,308
Total capitalization	793,070	766,589
Current liabilities		
Current maturities of Water System Revenue Bonds	4,325	26,155
Accounts payable	5,928	6,273
Accrued interest	8,769	9,666
Deferred revenue	1,000	1,000
Accrued retirement contributions	550	1,410
Accrued employee welfare	5,254	5,163
Other accrued liabilities	1,029	660
Customer deposits	5,694	5,799
Total current liabilities	32,549	56,126
Advances for construction	15,753	13,216
Deferred revenue	4,000	5,000
Commitments and contingencies (Note 10)		
	$845,372	$840,931

The accompanying notes are an integral part of these financial statements.

STATEMENT OF REVENUE AND REVENUE INVESTED IN FACILITIES

(Amounts in thousands)

	For the Year Ended May 31, 1999	1998
Revenue		
Operating	$ 96,962	$ 91,480
Interest and other	14,462	16,709
Total revenue	111,424	108,189
Operating expenses		
Operations	42,545	42,844
Maintenance	12,498	10,703
Total operating expenses	55,043	53,547
Revenue invested in facilities before depreciation, amortization, interest and extraordinary loss	56,381	54,642
Deduct:		
Interest expense, net	18,520	19,534
Depreciation and amortization	16,448	15,202
	34,968	34,736
Revenue invested in facilities before extraordinary loss	21,413	19,906
Extraordinary loss (Note 4)	831	2,210
Revenue invested in facilities	20,582	17,696
At beginning of year	185,308	167,612
At end of year	$205,890	$185,308

The accompanying notes are an integral part of these financial statements.

STATEMENT OF CASH FLOWS

(Amounts in thousands)

	For the Year Ended May 31, 1999	1998
Cash Flows from Operating Activities:		
Revenue invested in facilities	$ 20,582	$ 17,696
Adjustments to reconcile revenue invested in facilities to net cash (used in) provided by operations:		
Extraordinary loss	831	2,210
Depreciation and amortization	16,448	15,202
Capitalized interest	(927)	(1,420)
(Increase) decrease in operating assets:		
Short-term investments	(10,785)	(7,169)
Accounts receivable	506	(1,493)
Interest and other receivables	2,200	(1,482)
Accrued water service and fire protection revenues	(1,829)	(863)
Materials and supplies and prepayments	(7)	2,550
Other assets	1,862	8,628
Increase (decrease) in operating liabilities:		
Accounts payable	217	2,756
Accrued interest	(897)	706
Deferred revenue	(1,000)	(1,000)
Accrued retirement contributions	(860)	(307)
Deferred compensation fund	—	(6,636)
Accrued employee welfare	91	(597)
Other accrued liabilities	(193)	470
Customer deposits	(105)	(850)
Net cash (used in) provided by operating activities	26,134	28,401
Cash Flows from Investing Activities:		
Additions to water plant, net of retirements	(56,132)	(55,674)
Long-term investments	(27,060)	47,891
Decrease (increase) in construction fund	37,549	(18,184)
Net cash used in investing activities	(45,643)	(35,967)
Cash Flows from Capital Financing Activities:		
Proceeds from issuance of Water Systems Revenue Bonds	5,468	48,938
Defeasance of Series 1992 C Bonds	—	(38,655)
Defeasance of Series 1988 Bonds	(18,499)	—
Proceeds from notes payable	—	51,200
Repayment of notes payable	(4,800)	(42,100)
Repayment of current maturities of Water System Revenue Bonds	(8,195)	(7,470)
Advances for construction, net of refunds	11,733	12,413
Bond issuance costs	(250)	(833)
Funds held by fiscal agent	13	(1,583)
Net cash (used in) provided by capital financing activities	(14,530)	21,910
Net (decrease) increase in cash and cash equivalents	(34,039)	14,344
Cash and cash equivalents at beginning of year	39,569	25,225
Cash and cash equivalents at end of year	$ 5,530	$ 39,569

The accompanying notes are an integral part of these financial statements.

(Dollar amounts in thousands)

1. Summary of Significant Accounting Policies

Suffolk County Water Authority (the "Authority") is a public benefit corporation, created by resolution of the Suffolk County Board of Supervisors in 1937, with a two-fold purpose. The first was to acquire, construct, maintain and operate a public water supply for Suffolk County. The second was to develop a single, integrated public water supply and distribution system to serve all of Suffolk County. The accounts of the Authority are maintained generally in accordance with the Uniform System of Accounts prescribed by the New York State Public Service Commission ("PSC"), although the Authority is not subject to PSC rules and regulations. The rates established by the Authority do not require PSC or Suffolk County Legislative approval.

Acquisitions

In December 1997, the Authority acquired the portion of the Greenport water supply system existing outside the Greenport Village boundaries as well as a water tank for the aggregate purchase price of $3,500. The acquisition was accounted for as a purchase in accordance with Accounting Principles Board Opinion No. 16 and therefore, the results of operations of Greenport were included in the Company's financial statements beginning in December 1997, when the Authority began operating these facilities.

The aggregate purchase price of this water facility, which approximates fair value, was allocated to the net assets acquired in the water plant account.

Water Plant

Water plant is carried at original cost. The capitalized cost of additions to water plant include charges for ancillary construction costs such as construction period interest, engineering, supervision, payroll taxes and pension benefits. The original cost of property replaced, retired or otherwise disposed of in ordinary retirements is deducted from plant accounts and together with costs to remove, less any salvage, is charged to accumulated depreciation. The costs of repairs, minor betterments and renewals are charged to maintenance expense as incurred. The Authority does not credit water plant for contributions in aid of construction.

Depreciation

Depreciation of water plant is provided on the straight-line basis using a composite annual rate of 2.14%, which is based on the average service lives and net salvage values of properties.

Cash and Cash Equivalents

Investments which mature in ninety days or less are considered cash equivalents.

Funds Held by Fiscal Agent

The 1988 General Bond Resolution, as amended, (the "Resolution") requires that a debt service reserve fund (or bond insurance, as described in Note 4) be maintained and a bond fund be maintained by the Fiscal Agent.

The bond fund is used solely for the purpose of paying the principal and interest on the bonds, and for retiring the bonds prior to maturity. Amounts in the bond fund are invested in repurchase agreements and U.S. Treasury Notes.

Construction Fund

In accordance with the Resolution, monies in the construction fund are restricted to the costs of acquisition, construction and replacement of the water system.

Intangible Assets

Costs related to the issuance of long-term debt are amortized over the life of the issue, using the effective interest method.

Goodwill represents the excess of the purchase price over fair value of net assets acquired, and is being amortized over 40 years using the straight-line method.

Advances for Construction and Contributions in Aid of Construction

Under existing standard construction loan contracts with residential real estate developers and others, the developer advances to the Authority the estimated cost of new main installations. Upon completion of construction, the developer is either billed or refunded the difference between the advance and the actual cost. The resulting net completed cost is transferred to Contributions in Aid of Construction.

Contributions in Aid of Construction also includes the original cost of systems contributed to the Authority by municipalities and others as well as service, tapping and other fees.

The Federal Government has provided monies for certain water plant projects. The costs are billed and credited to Contributions in Aid of Construction upon submission to the Federal agency for reimbursement of expenditures made.

Beginning balance at May 31, 1998	$175,383
Federal monies expended	248
Other expenditures	8,948
Ending balance at May 31, 1999	$184,579

(Dollar amounts in thousands)

Customer Deposits

As security for the payment of bills, the Authority generally requires a deposit from commercial customers and large water users. No interest is paid on such deposits.

Prepayments

The Authority amortizes insurance premiums over the respective policy periods. With respect to workers compensation, the premiums are amortized over the claims period of 48 to 60 months. This resulted in a charge to insurance expense during the years ended May 31, 1999 and 1998 of $903 and $1,129 and a prepayment of $1,035 and $936 as of May 31, 1999 and 1998, respectively.

Compensated Absences

The Authority accrues the expected value of all vacation and sick leave benefits earned by employees to date.

Deferred Compensation

At June 1, 1997, the Authority adopted Governmental Accounting Standards Board Statement ("GASB") No. 32 "Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans" which establishes accounting and financial reporting standards for those deferred compensation plans of state and local governments that have changed the structure of the plans in accordance with IRC section 457 subsection (g)(1). IRC Code subsection requires that all assets and income of the plan be held in trust for the exclusive benefit of the participants and their beneficiaries. The effect of applying the statement resulted in the reduction of long-term assets and long-term liabilities in the amount of $6,636.

Revenue

Revenue is recognized based on actual customer water usage, including estimates for unbilled periods.

Income Taxes

As a public benefit corporation of the State of New York, the Authority is exempt from Federal, state and local income taxes.

Use of Estimates

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, as well as disclosures within the financial statements. Actual results could differ from those estimates.

Concentration of Credit Risk

Financial instruments which subject the Authority to credit risk consist principally of residential, commercial and industrial customer receivables. The Authority maintains reserves for potential credit losses from such accounts receivable and actual losses have historically not been materially different from management's estimates.

Reclassifications

Certain fiscal 1998 balances have been reclassified in order to conform with the current year presentation.

2. Water Plant

	May 31,	
	1999	1998
Land and land rights	**$ 15,700**	$ 15,497
Distribution systems	**538,594**	505,764
Wells, reservoirs and structures	**78,965**	73,370
Pumping and purification equipment	**84,771**	76,003
Other	**48,023**	44,641
Water plant in service	**766,053**	715,275
Less—accumulated depreciation	**174,955**	162,345
Net water plant in service	**591,098**	552,930
Construction in progress	**97,091**	93,515
Water plant	**$688,189**	$646,445

Depreciation expense amounted to $15,315 and $13,950 for the years ended May 31, 1999 and 1998, respectively.

3. Cash and Investments

Cash

Cash consists of insured (FDIC) or collateralized deposits which have carrying values of $5,530 and $39,569 and bank balances of $6,798 and $41,069 for the years ended May 31, 1999 and 1998, respectively.

Investments

Investments consist of the following:

	May 31, 1999		May 31, 1998	
	Carrying Amount	**Market Value**	Carrying Amount	Market Value
Certificates of Deposit	**$ 77,330**	**$ 77,330**	$ 29,797	$ 29,797
Funds Held by Fiscal Agent Repurchase Agreements	**17,010**	**17,010**	16,354	16,354
Funds Held by Fiscal Agent Other	**1,145**	**1,145**	1,814	1,814
Repurchase Agreements	**13,215**	**13,215**	23,699	23,699
Student Loan Marketing Association Medium Term Notes	**700**	**700**		
U.S. Treasury Bills	**293**	**293**	267	267
U.S. Treasury Notes			13,014	13,023
U.S. Government Discount Notes			24,465	25,000
Investments	**$109,693**	**$109,693**	$109,410	$109,954

Market values include accrued interest to the extent that it is in the carrying amounts. Accrued interest on investments other than Treasury Bills is included in interest and other receivables on the balance sheet. Investments bear interest rates that range from 4.53% to 6.55% and which mature at various dates through November 1999. It is the Authority's intent to hold all investments until maturity.

The Authority's investment policy states that securities underlying repurchase agreements must have a market value at least equal to the cost of the investment. All investments are either insured or registered and held by the Authority or its agent in the Authority's name. Accordingly, all investments are category-one credit risk (the lowest risk category).

The Authority's investment policies comply with the NYS Comptroller's guidelines for investment policies. Investment policies permit investments in, among others, obligations of the U.S. Treasury, its agencies, and repurchase agreements backed by such obligations.

4. Water Systems Revenue Bonds

Outstanding bonds are summarized as follows:

Series	Interest Rate	Final Maturity Date	May 31, 1998	Issued	Matured	Defeased	**May 31, 1999**
1988	6.50-7.375%	—	$ 22,715	$ —	$4,755	$17,960	**$ —**
1992 B	5.10-5.625%	2017	57,040	—	420	—	**56,620**
1993	4.80-5.10%	2013	87,310	—	2,770	—	**84,540**
1994	5.00-6.00%	2017	102,135	—	—	—	**102,135**
1997	4.10-5.30%	2012	38,470	—	—	—	**38,470**
1997 A	4.00-5.00%	2022	43,840	—	—	—	**43,840**
1998 B	3.60-5.20%	2017	6,192	—	250	—	**5,942**
1999 A	2.77-4.905%	2018	—	5,567	—	—	**5,567**
Less: amortized discount			7,049	99	324*	36	**6,788**
Total bonds outstanding			350,653	$5,468	$7,871	$17,924	**330,326**
Less: Current maturities payable			26,155				**4,325**
			$324,498				**$326,001**

*Includes current year amortization.

(Dollar amounts in thousands)

The payment of principal and interest of the Series 1992 B to 1999 A Bonds, is insured by a municipal bond insurance policy issued by MBIA Corporation or AMBAC Indemnity Corporation, except for the Series 1998 B and Series 1999 A Bonds, for which the Authority maintains the minimum debt service reserve fund balance.

During June 1998, the Authority defeased the remaining Series 1988 Water Systems Bonds in the amount of $17,960, by making a payment of $18,499 to an irrevocable trust held by the Authority's fiscal agent. The future cash flows from the Trust are equal to the scheduled interest and principal payments of the debt. The transaction effectively released the Authority from its obligation to repay the Series 1988 bonds and therefore, constituted a legal defeasance. The carrying amount of the bonds including current maturities, net of unamortized discount in the amount of $36 and unamortized bond issue costs in the amount of $256 was $17,668. The transaction resulted in an extraordinary loss of $831.

Interest expense was $16,793 and $17,547 for the years ended May 31, 1999 and 1998, respectively.

Bond maturities payable over the next five fiscal years are as follows:

Fiscal Year	Amount
2000	$ 4,325
2001	9,127
2002	9,590
2003	13,697
2004	14,330

5. Debt Service Requirements

As prescribed in the Authority's Resolution, a minimum debt service reserve fund balance is to be maintained, which is the lesser of 10% of the proceeds of the Series 1992 B-1999 A Bonds or the average of the annual installments of debt service with respect to all Series 1988-1999 A Bonds outstanding for the current and all future fiscal years. The Authority may purchase bond insurance in lieu of the debt service reserve fund requirement. The Authority has elected to maintain bond insurance on the Series 1992 B-1999 A Bonds, except for 1998 B and 1999 A Bonds, for the payment of principal and interest on stated maturity and sinking fund installment dates and in the event of default by the Authority. For the 1998 B and 1999 A Bonds, the Authority elected to maintain a minimum debt service fund balance of 10% of the proceeds.

Revenue before interest and depreciation was equivalent to 2.68 times (1.99 in 1998) the debt service requirement, for the year ended May 31, 1999. The minimum debt service requirement is 1.10.

6. Notes Payable

In May 1993, the Authority acquired Shorewood Water Corporation. In connection with the acquisition, the Authority issued a note payable to the former stockholders totaling $2,300. The note was repaid in fiscal year 1998.

In November 1997, February 1996 and December 1994, the Authority issued Bond Anticipation Notes (BANS) in the amounts of $51,200, $35,000 and $35,000, respectively. In February 1998, the entire balance of the BANS issued in 1994 was repaid. In May 1998, approximately $3,700 and $1,100 of the outstanding BANS issued in November 1997 and February 1996 were repaid. In May 1999, approximately $4,800 of the outstanding BANS issued in November 1997 were repaid. The remaining balance of BANS issued in 1997 and 1996 at May 31, 1999 was $42,700 and $33,900, respectively.

Interest on these notes is based on the minimum interest rate that, under prevailing financial market conditions, enables the notes to be sold at par, subject to the applicable effective interest rate period. The effective interest rate period may be daily, weekly, monthly, or semi-annually. Interest is payable periodically, based upon the effective interest rate period, through November 1, 2002, and February 8, 2001, the date of principal maturity, for the 1997 and 1996 notes, respectively.

As of May 31, 1999 and 1998, the effective interest rate was 3.07% and 3.58%, respectively.

Interest expense on the BANS was $2,479 and $3,296 for the years ended May 31, 1999 and 1998, respectively.

7. Pension Plan

The Authority's employees are eligible to participate in the New York State and Local Employees' Retirement System, which is a cost-sharing, multi-employer, public employee retirement system. The benefits provided to members of this retirement system are established by New York State law and may be amended only by the State Legislature. The New York State and Local Employees' Retirement System issues a publicly available financial report. The report may be obtained from the New York State and Local Retirement Systems, Gov. Smith State Office Building, Albany, New York 12244. Benefit provisions vary as follows:

The Employees' Retirement System is subdivided into the following four classes:

Tier I —members who last joined prior to July 1, 1973.
Tier II —members who last joined on or after July 1, 1973 and prior to July 27, 1976.
Tier III—members who last joined on or after July 27, 1976 and prior to September 1, 1983.
Tier IV—members who joined on or after September 1, 1983.

Tier I members are eligible for retirement at age 55. If members retire with 20 or more years of total service, the service retirement benefit is 2% of the final average salary for each year of service. If members retire with less than 20 years of total service, the service retirement benefit is 1.66% of the final average salary for each year of service.

Tier II members are eligible to retire with full benefits at age 62; and with reduced benefits for retirement between ages 55 and 62. Retirement benefits are equivalent to Tier I members.

Tier III members with 5 or more years of credited service after July 1, 1973, are eligible to retire with full benefits at age 62 or at age 55 with 30 years of service and with reduced benefits for retirement between ages 55 and 62 with less than 30 years of service. Benefits are integrated with Social Security beginning at age 62. If members retire at age 62 and have 25 or more years of credited service, the service retirement benefit will be 2% of final average salary for each year of service (not to exceed 30 years), plus 1.5% of the final average salary for each year of credited service beyond 30 years. If members retire at age 62 with fewer than 25 years of credited service, the service retirement benefit will be 1.66% of the final average salary for each year of service.

Tier IV members with 5 or more years of credited service are eligible to retire with full benefits at age 62 or at age 55 with 30 years of service and with reduced benefits for retirement between ages 55 and 62 with less than 30 years of service. Benefits are equivalent to Tier III members.

Retirement benefits vest after 5 years of credited service and are payable at age 55 or greater. The Employees' Retirement System also provides death and disability benefits.

Tier III and IV members are required by law to contribute 3% of their annual salary to the Employees' Retirement System and eligible Tier I and II members may make contributions under certain conditions. The Authority is required by the same statute to contribute the remaining amounts necessary to pay benefits when due.

Pension expense contractually required by New York State and recorded in the Authority's accounts was $332 and zero for the years ended May 31, 1999 and May 31, 1998. The zero amount of pension expense was the result of a change in the actuarial method utilized by New York State in 1994 in determining the contributions to be made to the Retirement System. The Authority has recorded an accrued retirement contributions liability for certain pensions costs of employees related to construction work in progress which have been capitalized to water plant.

8. Deferred Compensation

All Authority employees may participate in a deferred compensation program designated as an Internal Revenue Code Section 457 plan. This program enables employees to contribute a portion of their salary, on a tax deferred basis, to group variable annuity contracts. The assets and related liabilities of the plan are recorded at the assets' market values and are excluded from the Authority's balance sheet. The Authority has no liability to make contributions to the deferred compensation program. The Authority remits deferred compensation amounts withheld from employees' salaries to an outside fiduciary agent who administers the program and invests program assets as instructed by each of the participants. Assets in such program amounted to $10,432 and $8,381 at May 31, 1999 and May 31, 1998, respectively.

(Dollar amounts in thousands)

9. Postretirement Benefits

The Authority's employees participate in the New York State and Local Employees' Retirement system, a multi-employer plan, which provides certain health insurance benefits for retired employees. Substantially all the Authority's employees may become eligible for these benefits if they reach normal retirement age while working for the Authority. The cost of retiree health care benefits is recognized as an expense as costs are incurred. The expense amounted to $882 and $714 for the years ended May 31, 1999 and 1998, respectively.

10. Commitments and Contingencies

The Authority authorized a capital improvement construction budget for the fiscal year ending May 31, 2000 of approximately $38,989.

As of May 31, 1999, the Authority is obligated under several operating leases, for meter reading and computer equipment and under capital leases, for computer equipment, with initial or remaining terms of one year or more as follows:

Year ending May 31,	Operating	Capital
2000	$212	$169
2001	76	—
2002	66	—
2003	56	—
2004	2	—
	$412	$169
Less: amounts representing interest		5
Present value of minimum lease payments		164
Less: Current portion		164
		$ —

Rental expense for operating leases was $336 and $372 for the years ended May 31, 1999 and May 31, 1998, respectively.

The Authority is involved in various litigation resulting from the ordinary course of operations. In the opinion of management, and based on advice of legal counsel, the ultimate liability to the Authority which will result from the settlement of these matters will not have a material effect on the Authority's financial position, results of operations or cash flows.

Beginning in May 1997, the Authority began to address the issues surrounding the year 2000 and how it might affect the Authority's mission critical functions. Year 2000 issues result when computer program year dates are written in a two digit format, as opposed to four digit format (i.e., 99 instead of 1999). This can result in the year 2000, written in the two digit format of 00, being read as 1900, thus creating significant problems for date reliant and date sensitive programs and equipment. Significant time and resources have been dedicated by the Authority to identifying potential Year 2000 problem areas in our operations, correcting those problems, and testing implemented solutions. The Authority's Year 2000 plan addresses all information technology ("IT") systems, including proprietary and third party software, as well as non-IT systems, including the embedded technology in various devices operated by the Authority.

Early on, the issue of Year 2000 compliance was given high visibility within the Authority. The Chief Financial Officer and the Deputy Chief Executive Officer for Administration were designated Co-Chairs of the Authority's Year 2000 Task Force by the Chairman/CEO. Fiscal resources were fully committed and the Co-Chairs were given full capability to draw on any and all internal and external resources needed to achieve Year 2000 compliance. The initial Task Force consisted of senior managers and technical specialists from all of the Authority's major departments. Each department was responsible for identifying all date sensitive programs and equipment within its area, developing a plan and timetable to modify programs as required, and developing a program and timetable to replace equipment as required. This information was reported to the Task Force and monitored for progress. Each of the Authority's critical business and service processes is being reviewed to: identify and inventory sub-components; assess for Year 2000 compliance; establish repair plans as necessary and test in a Year 2000 environment. As of May 31, 1999, inventory, assessment, repair and testing for these service critical processes have been completed, with the exception of certain portions of the Authority's telephone system which will be replaced with Year 2000 compliant equipment at the end of the current lease in August. Progress reports have been made periodically to the Chairman of the Board. To date, the Authority has spent approximately $250,000 in hardware, software, and man hours to obtain Year 2000 compliance and additional costs are estimated to be $50,000.

Critical vendors and suppliers were also identified by the members of the Task Force and assurances of Year 2000 compliance were secured and documented.

Contingency planning is 50% complete, and is scheduled to be completed by September 30, 1999. Critical to the operation of our well sites is the availability of electricity to operate our water pumping wells. We have received assurances from the Long Island Power Authority and its business partner KeySpan that they are Year 2000 compliant and that electricity will be available and uninterrupted. In the unlikely event that electricity is lost in part or in whole, the Authority has sufficient backup generation to operate our water delivery system. In addition, the Authority's main campus has backup electrical generation capabilities which will enable our Information Service's mainframe computer and network servers to continue operation, and provide electrical power to our corporate headquarters and construction and maintenance group. Backup electrical generation capabilities also exist at our water quality laboratory, our customer service facility in central Suffolk County, and our production control facility. Fuel, which is critical to operate our backup electrical generation systems, is in sufficient supply in storage to operate our water production facilities until new deliveries of fuel are made. Our fuel vendors have certified that they are Year 2000 compliant.

The testing for communications systems has been completed with the exception of the Authority's telephone system, as discussed above. Our two-way radio communications system, which would play a major role in the event the Bell Atlantic system failed, does not have any date sensitive microprocessors. Radios are largely vehicle based with power from the vehicle. Base station radios are located at facilities with backup electrical generation. Sufficient cellular telephones exist in the event of a partial failure of the Bell Atlantic system, and use of satellite cellular telephones is currently being explored.

The Authority's water production facilities do not rely on date sensitive microprocessors. Chemical treatment done at our well sites does not have date sensitive microprocessors. The delivery system, which is largely interconnected, will allow water to be directed to various locations to maintain adequate pressures.

Sufficient staff will be on duty or on standby in the event of any date related occurrences. Officers of the Authority will be on duty to oversee and coordinate any required activities. We have had meetings with Suffolk County emergency preparedness representatives and we will coordinate our efforts with all appropriate governmental agencies.

While we believe that the Authority will be Year 2000 compliant, we cannot give assurance that the parties with whom the Authority does business will be Year 2000 ready. However, given the above described action we believe that we will continue to provide potable water in accordance with our rules and regulations.

REPORT OF INDEPENDENT ACCOUNTANTS

July 22, 1999

To the Members of
Suffolk County Water Authority

In our opinion, the accompanying balance sheet and the related statements of revenue and revenue invested in facilities and of cash flows present fairly, in all material respects, the financial position of Suffolk County Water Authority (the "Authority") at May 31, 1999 and 1998 and the results of its operations and its cash flows for the years then ended in conformity with generally accepted accounting principles. These financial statements are the responsibility of the Authority's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

The Year 2000 supplementary information on page 19 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board (GASB), and we did not audit and do not express an opinion on such information. Further, we were unable to apply to the information certain procedures required by professional standards because the disclosure criteria specified by GASB TB 98-1, as amended, are not sufficiently specific and, therefore, preclude the prescribed procedures from providing meaningful results. In addition, we do not provide assurance that the Authority is or will become Year 2000 compliant, that the Authority's Year 2000 remediation efforts will be successful in whole or in part, or that parties with which the Authority does business are or will become Year 2000 compliant.

PricewaterhouseCoopers LLP

PricewaterhouseCoopers LLP
Melville, New York


LEGEND
SCWA Service Areas
SCWA Non-Service Areas

REGIONAL OFFICES AND COMMUNITIES SERVED

Western Regional Office

REGIONAL MANAGER
Clifford Foy
260 Motor Parkway
Hauppauge, NY 11788

Amityville*
Asharoken
Babylon*
Bay Shore
Brentwood†
Centerport
Central Islip
Cherry Grove
Cold Spring Harbor
Commack
Copiague
Davis Park
Deer Park
Dix Hills†
East Islip
East Northport
Eaton's Neck
Edgewood
Fire Island Pines
Fort Salonga
Great River
Halesite
Hauppauge
Huntington
Huntington Station
Islip
Islip Terrace
Kings Park
Kismet
Lonelyville
Nesconset
North Amityville
North Babylon
North Great River
North Lindenhurst
Northport
Oakdale†
Point of Woods
St. James*†
Smithtown*†
Summer Club
Village of Babylon
Village of the Branch
Village of Brightwaters
Village of the Head of the Harbor
Village of Huntington Bay
Village of Islandia†
Village of Lindenhurst
Village of Nissequogue
Village of Northport
West Babylon
West Islip
Wheatley Heights
Wyandanch

Central Regional Office

REGIONAL MANAGER
Dona Roberts
2045 Route 112, Suite 1
Coram, NY 11727

Bayport
Bellport
Blue Point
Bohemia
Brookhaven
Centereach
Coram
East Patchogue
East Setauket
Farmingville
Gordon Heights
Holbrook
Holtsville
Lake Grove
Lake Panamoka
Lake Ronkonkoma
Medford
Middle Island
Miller Place
Mount Sinai
Oakdale†
Patchogue
Poquott
Port Jefferson
Port Jefferson Station
Ridge
Rocky Point
Ronkonkoma
Sayville
Selden
Setauket
Shoreham
Sound Beach
Stony Brook*†
Village of Belle Terre
Village of Bellport
Village of Islandia†
Village of Lake Grove
Village of Old Field
Village of Patchogue
Village of Port Jefferson
Village of Shoreham
Wading River
West Sayville
Yaphank

Eastern Regional Office

REGIONAL MANAGER
Steve Romano
1098 Old Riverhead Road
Westhampton Beach, NY 11978

Center Moriches
East Marion
East Moriches
Eastport
East Quogue
East Yaphank
Flanders
Greenport†
Laurel
Manorville
Mastic
Mastic Beach
Mattituck
Moriches
North Sea
North Shirley
Oakville
Orient
Quiogue
Quogue
Remsenburg
Riverside*
Shirley
Southampton
Southold
Speonk
Westhampton
Westhampton Beach

East Hampton

(Satellite Office—Eastern Regional Office)
Steve Romano
32 Montauk Highway
East Hampton, NY 11937

Amagansett
Bridgehampton
East Hampton
Montauk
North Haven
Sag Harbor
Sagaponack
Wainscott
Watermill

**Included in Wholesale Water District*

†Serves portion of area

GROUNDWATER GUARDIAN PROGRAM

We have continued our involvement with the Groundwater Foundation, a non-profit educational organization based in Lincoln, Nebraska.

Suffolk County was originally named as a Groundwater Guardian Community by the group in October 1998. This is a renewable designation, and the team that was originally assembled meets on a regular basis to reevaluate its primary concerns and develop and coordinate ways to address them. The team's current focus is on public education, pollution prevention, and other environmental concerns that could affect our groundwater. The seven-member group includes two SCWA staff members, a citizen activist, and representatives from local government, business, agriculture and education.

The Groundwater Guardian designation enables this area to join with hundreds of Groundwater Guardian communities throughout North America in a unified effort to motivate people to learn more about groundwater and help protect this essential resource.

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