



**Suffolk County Water Authority**  
2003 Annual Report

A large, leafy tree dominates the left and center of the frame. A person is sitting on the grass at the base of the tree, leaning against its trunk and reading a book. The scene is bathed in the warm, golden light of late afternoon or early morning, with the sun low on the horizon to the right, creating a lens flare effect. The background shows a grassy field and more trees under a bright sky.

# Stewardship

Ensuring a safe and plentiful water supply for generations to come

## 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 majority of the 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 52 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.

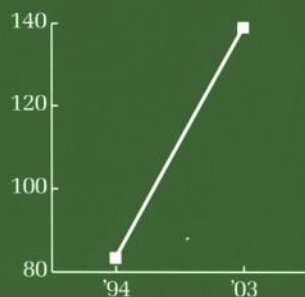
## Financial Highlights

	2003	1994	10-Year Growth	Percent Change
Customers .....	372,237	311,997	60,240	19%
Miles of Main.....	5,513	4,623	890	19%
Fire Hydrants.....	33,724	28,515	5,209	18%
Water Pumped (Billion Gallons).....	68.7	53.6	15	28%
Employees.....	567	593	(26)	-4%
Gross Revenues.....	\$ 139,061,000	\$ 83,430,000	\$ 55,631,000	67%
Expenses .....	70,340,000	51,910,000	18,430,000	36%
Water Plant at Cost .....	1,082,517,000	629,985,000	452,532,000	72%
Bonded Indebtedness .....	523,489,000	334,375,000	189,114,000	57%
Total Cumulative Earnings.....	281,987,000	135,714,000	146,273,000	108%

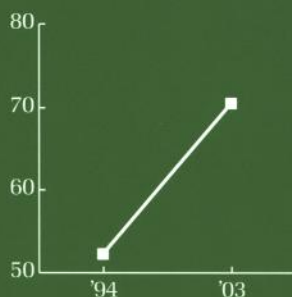
## 2002-2003 Highlights

	May 31, 2003	May 31, 2002
Total Revenues.....	\$ 139,061,000	\$ 128,195,000
Operating and Maintenance Expense.....	70,340,000	64,842,000
Interest on Bonds and Notes.....	16,257,000	21,196,000
Depreciation .....	25,575,000	18,265,000
Revenues Invested in Facilities		
before Extraordinary Loss .....	25,585,000	23,892,000
Extraordinary Loss .....	0	4,368,000
Revenues Invested in Facilities .....	25,585,000	19,524,000
Total Water Plant at Cost.....	1,082,517,000	1,029,304,000
Net Additions to Water Plant.....	53,213,000	57,672,000
Customers (Active Service).....	372,237	368,751
Miles of Main in Service.....	5,513	5,433
Fire Hydrants in Service .....	33,724	33,351
Water Production (Billion Gallons) .....	68.7	67.6

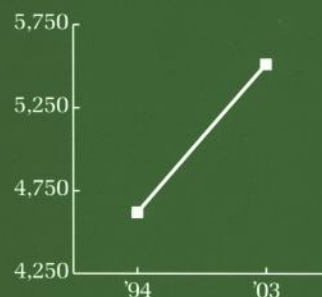
**Revenues**  
(dollars in millions)



**Expenses**  
(dollars in millions)



**Miles of Main**



# Stewardship is the responsibility to manage one's life and property with proper regard to the rights of others.

Over the past decade or so, the Water Authority has been at the forefront of protecting the aquifers from which we draw our water. We spearheaded the effort to protect and preserve the Central Pine Barrens of Suffolk County, an area critical to groundwater recharge. We successfully sued groundwater polluters to recover the cost of environmental remediation. We lobbied for the removal of groundwater contaminants such as the gasoline additive MTBE, providing expert testimony to a U.S. House of Representatives subcommittee. We supported and worked with local, county and state government for the preservation of land to preserve key watershed areas.

But the stewardship of our aquifers is not our responsibility alone. The total area of our customers' lawns and gardens is equal to the square mileage of Smithtown and Huntington Townships combined, and much of that area receives multiple applications of fertilizers, pesticides and herbicides. To make our customers "part of the solution," we began an education program to promote environmentally friendly lawn care and gardening techniques among our 372,000 customers using radio and print media, as well as our website, to disseminate information. Our in-school education program has now been incorporated into the curriculums of many schools in Suffolk County.

Through education, regulation, and cooperative efforts between various levels of government, and customer involvement, we have seen a marked improvement in our groundwater. Consider that fifteen years ago, over twenty percent of our wells required filtration to meet water quality standards. Today, less than ten percent of our wells require filtration to meet even more stringent standards. This is a significant accomplishment.

Stewardship is the responsibility to manage one's life and property with proper regard to the rights of others. Each of us has a role and a responsibility in protecting our groundwater, for ourselves, our children, and future generations.

# Chairman's Message

## Environmental Stewardship and Financial Responsibility

Fifty-two years ago when the Water Authority first began operations, its focus was on the immediate need to bring safe and reliable drinking water to the more populated areas of the Suffolk County. With the first acquisition of the systems of the South Bay Water Company in the Babylon area, the Water Authority began a long and proud tradition of serving the people of Suffolk County. During the first forty years of our existence, we measured our success by the miles of water main installed, the number of new wells drilled, the gallons of water pumped, and the number of new customers added. But as we learned more about the sole source aquifer system from which we draw our water and the impact that pumping water and surface land use have on these aquifers, and as federal and state water quality regulations tightened, we began to set a new course for the Water Authority. While drinking water quality, and the Authority's fiscal strength and responsibility will always be our top priorities, we realized that we had to take on the responsibility of stewardship of our aquifer systems to ensure the quality and quantity of the water we supply for our current customers and for future generations. No longer could we be just a supplier of water, no longer could we measure our success only in completed construction and water sales, our direction, our very mission had broadened and changed. Some have referred to this new sense of responsibility as the "Greening of the Water Authority"; we view it as a logical extension of our serious and ongoing responsibility to deliver pure, safe, and reliable drinking water to the 1.2 million people we serve in Suffolk County.

Our first foray in this new direction, over a decade ago, brought us together with new partners to ensure the preservation of Suffolk County's Central Pine Barrens, an

area critical to the deep recharge of our water supply. We brought together diverse interests and formed many new alliances and, in the end, helped to save this critical recharge area from development. Since that time, our efforts have continued to focus on responsibly addressing future

water supply needs through comprehensive planning. During this fiscal year, we provided a matching grant to the Town of Shelter Island to study its long-term water needs, and to determine if there was a role for the Water Authority to supply water to this area either on a retail or wholesale basis. Also during this period, we completed a Final Generic Environmental Impact Statement for our North Fork operation to provide a framework for supplying public water to this area over the next five years in an environmentally sensitive and fiscally responsible manner. This study considered various supply options and the financial implications of each, including treatment of local supplies as well as importing water from areas west of Southold. Future expansion of our system will be driven by population growth and development, both of which will be determined solely by the Town of Southold government. We will continue to respect their comprehensive planning initiatives and concentrate on bringing drinking water to residents on private wells.

Because we want our stewardship to involve neighborhoods and communities, the Water Authority implemented several community-based programs under our Good Neighbor Initiative. This year we began our Community Arboretum Program. Using the open and protected expanses of our well fields in communities throughout Suffolk County, we began to plant large specimen trees in open areas that will allow the trees to grow to their full size and beauty unencumbered. Our plan is to continue these plantings over the years to beautify our well fields and the communities in which they are located. It is one way we are rewarding our pump station neighbors for keeping an eye on our facilities for us when we're not there. Working with Dark Skies, a national group dedicated to reducing light pollution, we retrofitted the outdoor lighting systems at our East Hampton and Westhampton facilities to reduce nighttime glare and extraneous lighting. Based upon the successful results of these two projects, we are continuing to retrofit other facilities without adversely affecting either safety or security. Our Community Gardens Program makes public water available at a nominal fee to groups planting and tending gardens in public areas and several public gardens have successfully been developed and flourish under this program.



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Our **stewardship** extends beyond environmental concerns and encompasses the fiscal strength of the Water Authority itself.



*Michael A. LoGrande, Chairman*

Leading by example, the Water Authority has initiated several projects to protect our environment. Large underground fuel storage tanks located at several of our operations facilities are being replaced with state-of-the-art tanks and monitoring devices well in advance of New York State's deadline of 2010. We have begun work with various environmental groups to re-landscape our Eastern Regional Office, which is located in the globally-rare dwarf pine plains in Westhampton, with native to Long Island plantings using xeriscaping techniques and expect to complete this project by the spring of 2004. We are continuing to experiment with organic lawn care techniques at our major facilities and scientifically study its effects upon nitrates in subsurface soils in conjunction with the Stony Brook University Groundwater Research Institute. And finally, we are continuing to promote both organic lawn care techniques as well as odd-even watering to our customers through both print and radio media.

But our stewardship extends beyond environmental concerns and encompasses the fiscal strength of the Water Authority itself. Without that strength, and the trust and faith of our bondholders, many of our advances and progressive initiatives over the past ten years would not have been possible.

In July 2003, the financial community spoke loudly when Standard & Poor's and Moody's Investor Services reaffirmed the Water Authority's strong financial ratings of AA- and Aa, respectively, the highest bond rating of any revenue-based Authority in New York State. This high rating will save our customers millions of dollars in future years as continued customer growth, averaging 4,000 customers annually, will require some borrowing for construction.

Several new financial challenges and opportunities were addressed this year. To help finance our continuing construction program (\$50.2 million in fiscal year ending May 2003) in a time of a continued weak economy and low interest rates, we issued \$70 million in variable rate notes paying an average interest rate of approximately 1%. We also continued our participation in the New York State Drinking Water Revolving Fund by borrowing \$8.6 million of fixed long-term debt at an average interest rate of 3.91%. These financing techniques allowed us to minimize debt service, maximize debt service coverage, and maintain one of the lowest water rates in the country. In addition,

\$67 million and \$80 million of long-term fixed rate bonds were issued subsequent to the end of the fiscal year (June and July 2003) at average interest rates of 3.15% and 4.54%, respectively, for the purpose of refunding higher interest rate long-term bonds and locking in a low interest rate on \$82,000,000 of outstanding variable rate debt.

Although the economy has been weak and inflation low, operating expenses have risen at an above average rate due to increased water consumption, wages, security concerns and fringe benefits such as health insurance and pension costs. Forty employees opted to take an early retirement incentive, costing \$2.6 million. This cost, however, will be offset with operational savings in the next two years exceeding this amount. The New York State Retirement System, in which the Authority participates, has increased its normal contribution requirements, which will cost the Authority \$2 to \$3 million more annually. Many municipalities in the system are struggling to meet their budgetary requirements. However, our long-term prudent fiscal management will allow us to manage these expenses with minimal impact. Active employer pension costs are expected to increase for several years due to the impact of the investment markets on the New York State Retirement System.

This year's financial statement includes "Management's Discussion and Analysis" of financial activity, as required by the Government Accounting Standards Board, resulting in more detailed disclosure of financial activity. As a quasi-municipal enterprise operation, we follow both Generally Accepted Accounting Principles and Government Financial Standards Board Pronouncements. Our historically conservative approach and strong financial standing are reflected by both of these standards.

To the financial community, we commit to continue our conservative financial approach, to maintain strong debt service coverage, and our high bond rating. To our customers and their families, we commit to maintain the lowest possible water rates, excellent service, and above all else, water that is pure and safe to drink.

A handwritten signature in cursive script that reads "Michael A. LoGrande".

Michael A. LoGrande  
*Chairman*



Community and classroom based education programs are an important part of our outreach to our customers and their families.

## Management's Discussion and Analysis

### May 31, 2003 and 2002

During the fiscal year ended May 31, 2003, the Authority adopted Governmental Accounting Standards Board ("GASB") Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments," as amended by GASB Statement No. 37 "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus" and GASB Statement No. 38, "Certain Financial Statement Note Disclosures." GASB Statement No. 34 establishes accounting and financial reporting standards for general purpose external reporting by state and local governments and requires, among other things, that Management's Discussion and Analysis be included as required supplemental information to the general purpose external financial statements.

As a result of the adoption of GASB Statement No. 34 and its subsequent interpretations by the Suffolk County Water Authority (the "Authority") during the current year, the Authority has changed the presentation of its financial position, results of operations and cash flows in its general purpose external financial statements. The prior year financial statements have been restated to conform to the current year presentation.

Management provides the following discussion and analysis ("MD&A") of the Authority's financial activities and statements. This overview is provided for the fiscal years ended May 31, 2003 and 2002. The reader should use the information contained in this analysis in conjunction with the information contained in our audited financial statements all of which follow this narrative on the subsequent pages.

#### FINANCIAL HIGHLIGHTS

<i>(in thousands of dollars)</i>	2003	2002
<b>Operating revenues</b>		
Water service .....	<b>\$114,106</b>	\$108,800
Other .....	<b>9,588</b>	8,193
Total operating revenues .....	<b>123,694</b>	116,993
<b>Operating expenses</b>		
Operations and maintenance .....	<b>70,340</b>	64,842
Depreciation and amortization .....	<b>26,879</b>	19,467
Total operating expenses .....	<b>97,219</b>	84,309
Operating income .....	<b>26,475</b>	32,684
<b>Non-operating revenues and expenses</b>		
Interest expense, net .....	<b>(12,057)</b>	(12,021)
Capital reimbursement fees .....	<b>11,167</b>	15,631
Total non-operating revenues and expenses .....	<b>(890)</b>	3,610
Income before special item .....	<b>25,585</b>	36,294
Loss on extinguishment of debt .....	<b>—</b>	(4,368)
Increase in net assets .....	<b>\$ 25,585</b>	\$ 31,926

#### Operating Revenues

Water service revenues increased \$5.3 million or 4.9% during the current year from \$108.8 million for the 2002 fiscal year to \$114.1 million for the 2003 fiscal year. The increase was a result of customer growth, dry weather conditions, and the increased use of in-ground water sprinkler systems.

Other operating revenues increased \$1.4 million or 17% from \$8.2 million for the 2002 fiscal year to \$9.6 million for the 2003 fiscal year. The \$1.4 million increase is primarily attributable to a \$1.1 million increase in rental income from antennae leases as a result of continued growth in the cell phone industry resulting in communication companies seeking additional space on Authority property for transmission equipment.

#### Operating Expenses

Operations and maintenance expense increased \$5.5 million or 8.5% from \$64.8 million for the 2002 fiscal year to \$70.3 million for the 2003 fiscal year. The \$5.5 million increase was attributable to increased health care costs (\$.7 million), workers' compensation costs (\$1.5 million), retirement costs (\$1.8 million), power costs (\$1.1 million), and maintenance costs (\$.4 million).

Depreciation and amortization expenses were \$26.9 million during fiscal 2003 as compared to \$19.5 million during fiscal 2002, an increase of \$7.4 million or 38.1% during the current year. The increase in depreciation and amortization was primarily attributable to an increase in depreciable water plant assets coupled with an increase in the composite rate for depreciation. During the current year, the Authority engaged outside consultants to perform a depreciation study that yielded an increase in the composite rate of .70 percentage points from 2.14% during fiscal 2002 to 2.84% during fiscal 2003.

#### Non-Operating Revenues (Expenses)

Capital reimbursement fees were \$11.2 million during fiscal 2003 as compared to \$15.6 million during fiscal 2002, a decrease of \$4.4 million or 28.6% during the current year. Capital reimbursement fees include developer fees, (which are initially recognized as construction advances), tapping fees, and other capital reimbursement surcharges. As projects are closed these funds are transferred from the construction advances to the capital reimbursement fee account. Fewer developer construction projects initiated over the past couple of years has resulted in a decline in the amount of monies being transferred from the advance account and being recognized as income when projects are closed. During fiscal years ending May 31, 2003 and 2002, the amount of monies transferred were \$4.4 million and \$7.8 million, respectively, a decrease of \$3.4 million.



Interest expense was \$16.3 million during fiscal 2003 as compared to \$20 million during fiscal 2002, a decrease of \$3.7 million, which is attributable to the defeasance of \$72.3 million of certain Senior Lien Water Revenue Bonds, Series 1992 A&B and Series 1993 in March, 2002.

Interest income was \$4.2 million during fiscal 2003 as compared to \$8 million during fiscal 2002, a decrease of \$3.8 million, which is attributable to the lower interest yields for invested funds.

### Summary of Financial Position

<i>(in thousands of dollars)</i>	2003	2002
<b>Assets</b>		
Capital assets.....	\$ 839,224	\$ 808,613
Other assets		
Current .....	104,436	103,724
Long-term .....	143,870	111,441
Total current assets .....	1,087,530	1,023,778
<b>Liabilities</b>		
Current liabilities.....	44,338	70,092
Other long-term liabilities.....	16,640	19,276
Long-term debt.....	515,049	448,492
Total current liabilities.....	576,027	537,860
<b>Net assets</b>		
Invested in capital, net of related debt .....	390,936	339,705
Restricted for debt service.....	22,912	24,668
Unrestricted .....	97,655	121,545
Total net assets.....	511,503	485,918
Total liabilities and net assets.....	\$1,087,530	\$1,023,778

### Capital Assets (Water Plant)

There was a net increase in water plant of \$30.6 million comprised of an increase in gross water plant (including construction in progress) of \$53.2 million reduced by an increase in accumulated depreciation of \$22.6 million. Refer to Notes to Financial Statements for further details concerning capital asset activities.

### Current Assets

The components of the \$712 thousand increase in current assets are as follows:

<i>(in thousands of dollars)</i>	
<b>Increases</b>	
Current portion of investments .....	\$4,481
Accounts receivable, net.....	98
Interest and other receivables.....	104
Materials and supplies.....	845
	5,528
<b>Decreases</b>	
Cash and cash equivalents.....	2,600
Accrued water services and fire protection.....	1,792
Prepayments and other current assets .....	424
	4,816
Net increase in current assets.....	\$ 712

The \$2.6 million decrease in cash and cash equivalents was attributable to cash used in capital related financing activities of \$74.1 million offset by cash provided by operating activities of \$61.5 million and cash provided by investing activities of \$10 million.

Accrued water services and fire protection reflects accrued revenue corresponding to pumpage, which has not been billed as of May 31st. High rainfall in April and May of 2003 resulted in lower pumpage than the comparative period of 2002. Consequently, the accrued water service and fire protection account at May 31, 2003 is down \$1.8 million in comparison to 2002.

### Non-Current Assets

The value of non-current assets increased by approximately \$32.4 million, which is comprised of a \$41.4 million increase in construction funds and a \$3.2 million increase in deferred charges and other assets offset by a \$10.4 million decrease in non-current investments and a \$1.8 million decrease in debt service reserve and bonds.

Monies in the construction fund are internally designated to the costs of acquiring, constructing and replacing the water system. The increase in construction funds is a result of additional financing received, which is designated for construction projects. Refer to Long-Term Debt discussions for detailed information.

The increase in deferred charges and other assets is due primarily to an increase of \$3.6 million due from the Town of Islip for the installation of main in the community of Fair Harbor, Fire Island, New York. The Authority and Town of Islip have an agreement for the cost to be paid back over a twenty (20) year period, with interest. The increase in the Town of Islip receivable was offset by a \$425 thousand decrease in other assets.

### Investments

Investments are classified as both long-term and short-term based upon the dates of maturity on the instruments with consideration given to the Authority's reasonable expectation of those resources to be consumed during a normal operating cycle. The Authority's investments decreased \$5.8 million or 6.30% from \$92.7 million as of May 31, 2002 to \$86.9 million as of May 31, 2003. The decrease in investments overall is attributable primarily to the utilization of the Authority's General Fund to pay off \$28.1 million of Bond Anticipation Notes—1997 offset by the addition of funds available from revenues after the payment of debt service.

### Current Liabilities

The \$25.8 million decrease in current liabilities is primarily the result of repayment of \$32.3 million on the 1997 variable rate Bond Anticipation Notes which came due during the current year, a decrease in accrued interest of \$349 thousand and a decrease in accrued employee welfare of \$328 thousand. These decreases were offset by increases in accounts payable (\$1.1 million), other accrued

liabilities (\$3 million), accrued retirement contributions (\$2.6 million) and customer deposits (\$452 thousand).

Accrued retirement contributions have increased approximately \$2.6 million. During the current year, the Authority participated in the 2002 New York State Retirement Incentive Program. Forty (40) employees took part in this program retiring by December 31, 2002. The estimated cost to SCWA is \$2.6 million. The Authority is evaluating each position of those retirees and where applicable not filling the position. Those positions required will in most cases be filled at lower salaries. The Authority anticipates payroll savings in excess of \$2.6 million over a two (2) year period ending December 31, 2004. The Authority has been advised by the NYS Retirement System regular pension costs for the current fiscal year to be 4.5% of payroll as compared to 0.5% for the last fiscal year. The liability reflected in the Authority's balance sheet as of May 31, 2003 is \$2.9 million, an increase of \$2.6 million over last year's liability.

The \$1.1 million increase experienced in accounts payable is attributable principally to an increase in outstanding invoices related to construction (\$1.2 million), reduction in outstanding operating and maintenance invoices (-\$.4 million) and an increase in accounts receivable credits in the amount of \$.3 million.

The increase of \$3 million experienced in other accrued liabilities is primarily attributable to a \$2.9 million increase in insurance reserves for workers' compensation and auto damage claims as a result of establishing an additional reserve for potential costs to current and past workers' compensation claims.

The following table sets forth the Authority's outstanding Long-Term Bonds and Variable Rate Bond Anticipation Notes as of May 31, 2003 and 2002:

<i>(in thousands of dollars)</i>	Original Principal Amount	Principal Outstanding at May 31, 2003	Principal Outstanding at May 31, 2002
<b>Senior Lien Bonds</b>			
Water System Revenue Bonds, Series 1993, Refunding, dated March 15, 1993.....	\$70,135	\$ 41,445	\$ 41,445
Water System Revenue Bonds, Series 1994, dated January 1, 1994.....	64,000	64,000	64,000
Water System Revenue Bonds, Series 1997, dated March 1, 1997.....	38,470	32,530	33,955
Water System Revenue Bonds, Series 1997A, dated November 1, 1997.....	43,840	38,230	41,230
Water System Revenue Bonds, Series 1998B (EFC Series), dated March 15, 1998.....	6,192	5,020	5,255
Water System Revenue Bonds, Series 1999A (EFC Series), dated March 3, 1999.....	5,567	4,765	4,977
Water System Revenue Bonds, Series 2000A (EFC Series), dated March 9, 2000.....	876	780	810
Water System Revenue Bonds, Series 2000B (EFC Series), dated July 27, 2000.....	5,359	5,024	5,194
Water System Revenue Bonds, Series 2001A, dated March 8, 2001.....	38,200	38,200	38,200
Water System Revenue Bonds, Series 2001A (EFC Series), dated March 8, 2001.....	10,629	9,725	10,089
Water System Revenue Bonds, Series 2001B (EFC Series), dated July 26, 2001.....	17,633	16,352	16,964
Water System Revenue Bonds, Series 2002A (EFC Series), dated March 14, 2002.....	10,869	10,294	10,594
Water System Revenue Bonds, Series 2002B (EFC Series), dated July 25, 2002.....	8,614	8,385	—
Total outstanding Senior Lien Bonds.....		<b>\$274,750</b>	\$272,713
<b>Subordinate Lien Bonds</b>			
Water System Revenue Bonds, Series 1993			
Subordinate Lien Refunding, dated March 15, 1993.....	\$28,415	\$ 15,385	\$ 15,925
Water System Revenue Bonds, Series 1994			
Subordinate Lien Refunding, dated February 15, 1994.....	38,135	33,541	34,985
Total outstanding Subordinate Lien Bonds.....		<b>\$ 48,926</b>	\$ 50,910

## LONG-TERM DEBT

The Authority's long-term debt (including current maturities and exclusive of unamortized discounts) increased by \$33.8 million comprised of a \$50 thousand increase in bonds and a \$33.7 million increase in variable rate bond anticipation notes ("BANs") detailed as follows:

### Water System Revenue and Environmental Facilities Corporation Revenue Bonds

*(in thousands of dollars)*

<b>New Issue</b>	
EFC 2002B.....	\$ 8,615
1993 Jr. ....	(540)
1994 Jr. ....	(1,445)
1997.....	(1,425)
1997A.....	(3,000)
EFC 1998B.....	(235)
EFC 1999A.....	(212)
EFC 2000A.....	(30)
EFC 2000B.....	(170)
EFC 2001A.....	(365)
EFC 2001B.....	(613)
EFC 2002A.....	(300)
EFC 2002B.....	(230)
Net change in long-term debt.....	\$ 50
<b>BANs</b>	
BANs 2003.....	\$ 70,000
BANs 1997.....	(32,300)
BANs 2000.....	(2,100)
BANs 2001.....	(1,900)
Net change in variable rate BANs.....	\$ 33,700

The Authority has issued from time to time bond anticipation notes to finance improvements and additions to the Water System. As of May 31, 2003 and 2002, the Authority had the following bond anticipation notes outstanding:

<i>(in thousands of dollars)</i>	Original Principal Amount	Principal Outstanding at May 31, 2003	Principal Outstanding at May 31, 2002
Variable Rate Bond Anticipation Notes, 1997, dated November 13, 1997, maturing November 1, 2002.....	\$51,200	—	\$ 32,300
Variable Rate Bond Anticipation Notes, 2000, dated May 2, 2000, maturing May 1, 2005 .....	50,000	<b>\$ 46,000</b>	48,100
Variable Rate Bond Anticipation Notes, 2001, dated June 27, 2001, maturing June 1, 2006 .....	90,000	<b>88,100</b>	90,000
Variable Rate Bond Anticipation Notes, 2003, dated January 29, 2003, maturing January 1, 2008 .....	70,000	<b>70,000</b>	—
Total outstanding Bond Anticipation Notes.....		<b>\$204,100</b>	\$170,400

In June 2003, the Authority determined it advisable and financially advantageous to issue on June 19, 2003 \$67,395,000 of Senior Lien Bonds, Water System Revenue Bonds, Series 2003 (Refunding) to provide for the refunding, in advance of their maturities all of the \$64 million of its Water System Revenue Bonds, Series 1994, dated January 1, 1994, \$2,575,000 of its Water System Revenue Bonds, Series 1997, dated March 1, 1997, maturing June 1, 2004, and \$1,550,000 of its Water System Revenue Bonds, Series 1997A, dated November 1, 1997, maturing June 1, 2004. These bonds bear interest at rates ranging from 2% to 4.5% and have a final maturity date of June 1, 2017.

In July 2003, the Authority determined it advisable and financially advantageous to issue on July 24, 2003 \$80,000,000 of Senior Lien Bonds, Water System Revenue Bonds, Series 2003C to provide for the retirement of \$45,900,000 aggregate principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2000 and \$33,200,000 aggregate principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2001. These bonds bear interest at rates ranging from 4% to 4.75% and have a final maturity date of June 1, 2026.

As a result of legislation initiated by New York State and enacted by the U.S. Congress a Drinking Water State Revolving Fund ("DWSRF") was created to provide financial incentive for public and private water systems to finance drinking water infrastructure improvements in the form of subsidized low interest rate loans and grants for qualified projects. The Environmental Facilities Corporation ("EFC") administers the financial aspects of the DWSRF. The Authority has participated in this program since 1998.

The Authority has determined it advisable and financially advantageous to continue to borrow from the Environmental Facilities Corporation and in July 2003 issued \$9,130,775 of Senior Lien Bonds to provide for the retirement of \$100,000 principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2000, retirement of \$2,800,000 principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2001, to fund a reserve account for these Senior Lien Bonds in the amount of \$913,078, and to finance additional costs of the approved projects.

#### CREDIT RATING

In July 2003, Standard & Poor's and Moody's Investors Service affirmed ratings of AA- and Aa on Suffolk County Water Authority debt.

#### FINANCIAL STATEMENT PRESENTATION

The Authority's financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. The transactions of the Authority are accounted for on a flow of economic resources measurement focus.

#### REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of the Suffolk County Water Authority's finances for all those interested. Questions concerning any of the information provided in this report or requests for additional information should be addressed in writing to the Chief Financial Officer, Suffolk County Water Authority, P.O. Box 37, Oakdale, New York 11769.

## Balance Sheets

May 31, 2003 and 2002

(in thousands of dollars)

	2003	2002
<b>ASSETS</b>		
Water plant, at cost less accumulated depreciation .....	\$ 839,224	\$ 808,613
Current assets		
Cash and cash equivalents .....	1,990	4,590
Investments .....	72,786	68,305
Accounts receivable, less allowance for doubtful accounts of \$738 and \$849 in 2003 and 2002, respectively .....	9,411	9,313
Accrued water services and fire protection revenues .....	12,196	13,988
Interest and other receivables .....	965	861
Materials and supplies, at average cost .....	5,395	4,550
Prepayments and other current assets .....	1,693	2,117
Total current assets .....	104,436	103,724
Investments .....	14,074	24,423
Debt service reserve and bond funds .....	22,912	24,668
Construction fund .....	94,146	52,776
Goodwill .....	4,839	4,839
Deferred charges and other assets .....	7,899	4,735
	143,870	111,441
Total assets .....	\$1,087,530	\$1,023,778
<b>LIABILITIES</b>		
Current maturities on bond anticipation notes payable .....	—	32,300
Current maturities of bonds payable .....	8,440	8,408
Accounts payable .....	7,139	6,020
Accrued interest .....	7,051	7,400
Accrued employee welfare costs .....	5,383	5,711
Other accrued liabilities .....	7,084	4,101
Customer deposits .....	5,340	4,888
Deferred revenue .....	1,000	1,000
Accrued retirement contributions .....	2,901	264
Total current liabilities .....	44,338	70,092
Commitments and contingencies		
Bond anticipation notes payable .....	204,100	138,100
Bonds payable, less current portion and unamortized discount .....	310,949	310,392
Obligation under capital lease .....	425	582
Advances for construction .....	16,215	17,694
Deferred revenue .....	—	1,000
Total liabilities .....	576,027	537,860
<b>Net assets</b>		
Invested in capital, net of related debt .....	390,936	339,705
Restricted for debt service .....	22,912	24,668
Unrestricted .....	97,655	121,545
Total net assets .....	511,503	485,918
Total capitalization and liabilities .....	\$1,087,530	\$1,023,778

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

## Statements of Revenues, Expenses and Changes in Net Assets

Years Ended May 31, 2003 and 2002

(in thousands of dollars)

	2003	2002
<b>Operating revenues</b>		
Water service .....	\$114,106	\$108,800
Other .....	9,588	8,193
Total operating revenues .....	123,694	116,993
<b>Operating expenses</b>		
Operations .....	53,906	48,850
Maintenance .....	16,434	15,992
Depreciation and amortization .....	26,879	19,467
Total operating expenses .....	97,219	84,309
Operating income.....	26,475	32,684
<b>Non-operating revenues and expenses</b>		
Interest expense .....	(16,257)	(19,994)
Interest income.....	4,200	7,973
Capital reimbursement fees .....	11,167	15,631
Total non-operating revenues and expenses .....	(890)	3,610
Income before special item.....	25,585	36,294
Loss on extinguishment of debt .....	—	(4,368)
Increase in net assets .....	\$ 25,585	\$ 31,926
<b>Net assets</b>		
Beginning of year .....	485,918	453,992
End of year .....	\$511,503	\$485,918

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

## Statements of Cash Flows

### Years Ended May 31, 2003 and 2002

(in thousands of dollars)

	2003	2002
<b>Cash flows from operating activities</b>		
Cash receipts from customers .....	\$115,176	\$110,585
Other operating cash receipts.....	9,386	8,237
Cash payments to suppliers of goods and services.....	(35,863)	(39,854)
Cash payments to employees for services .....	(27,141)	(25,548)
Net cash provided by operating activities .....	61,558	53,420
<b>Cash flows from investing activities</b>		
Net proceeds from sales/(purchases) of investment securities.....	5,869	13,115
Interest received.....	4,097	8,070
Net cash provided by investing activities .....	9,966	21,185
<b>Cash flows from capital and related financing activities</b>		
Defeasance of bonds payable.....	—	(75,328)
Additions to water plant, net of retirements.....	(56,509)	(57,522)
Designations to the construction fund.....	(41,370)	(30,377)
Proceeds from issuance of EFC Bonds.....	8,615	28,402
Proceeds from issuance of notes payable .....	70,000	89,543
Repayment of notes payable.....	(36,300)	(10,100)
Repayment of current maturities of Bonds payable.....	(8,564)	(11,025)
Interest paid .....	(16,606)	(21,780)
Repayment of capital lease obligation .....	(157)	(217)
Proceeds from advances for construction, net of refunds .....	5,827	14,178
Payment of bonds and notes payable issuance costs.....	(815)	(853)
Designations to the debt service reserve and bond funds .....	1,755	1,101
Net cash used in capital and related financing activities.....	(74,124)	(73,978)
Net (decrease) increase in cash and cash equivalents .....	(2,600)	627
Cash and cash equivalents at beginning of year .....	4,590	3,963
Cash and cash equivalents at end of year.....	\$ 1,990	\$ 4,590
<b>Reconciliation of operating income to net cash provided by operating activities</b>		
Operating income.....	\$ 26,475	\$ 32,684
Depreciation and amortization expense .....	26,879	19,467
(Increase) decrease in operating assets		
Accounts receivable.....	(652)	(139)
Accrued water service and fire protection .....	1,792	2,398
Materials and supplies and prepayments.....	(422)	(583)
Other assets .....	797	1,044
Increase (decrease) in operating liabilities		
Accounts payable.....	1,946	(1,501)
Accrued retirement contribution .....	2,636	(138)
Deferred revenue.....	(1,000)	(1,000)
Accrued employee welfare.....	(328)	303
Other accrued liabilities .....	2,983	1,117
Customer deposits.....	452	(232)
Net cash provided by operating activities .....	\$ 61,558	\$ 53,420

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

# Notes to Financial Statements

## May 31, 2003 and 2002

### 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.

#### Basis of Presentation

The Authority's financial statements are prepared in accordance with all applicable pronouncements of the Governmental Accounting Standards Board ("GASB"). In accordance with GASB Statement No. 34, "Basic Financial Statements and Management Discussion and Analysis for State and Local Governments" ("GASB 34"), the Authority also prepares its financial statements in accordance with all authoritative pronouncements applicable to non-governmental entities (i.e., Financial Accounting Standards Board ("FASB") statements) that do not conflict with GASB pronouncements.

During fiscal 2003, the Authority adopted GASB 34, as amended by GASB Statement No. 37, "Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments: Omnibus," and GASB Statement No. 38, "Certain Financial Statement Note Disclosures." GASB 34 establishes accounting and financial reporting standards for general purpose external reporting by state and local governments and requires, among other things, that Management's Discussion and Analysis be included as required supplemental information to the general purpose external financial statements. GASB 34 further requires the classification of net assets into three components: invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

#### *Invested in capital assets, net of related debt*

This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and 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. If there are significant unspent related debt proceeds at year end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.

#### *Restricted net assets*

This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

#### *Unrestricted net assets*

This component of net asset consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

In accordance with GASB 34, the accounting and financial reporting treatment applied to the Authority is determined by its measurement focus and the transactions of the Authority are accounted for on a flow of economic resources measurement focus and accrual basis of accounting.

As a result of the adoption of GASB 34 and its subsequent interpretations, during the current year, the Authority has changed the presentation of its financial position, results of operations and cash flows in its general purpose external financial statements. The prior year financial statements have been restated to conform with the current year presentation.

#### Water Plant

Water plant is recorded 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.

#### Depreciation

Depreciation of water plant is provided on the straight-line basis using a composite annual rate of 2.84% (2.14% during fiscal 2002), which is based on the average service lives and net salvage values of properties.

During the current year, the Authority engaged an outside consultant to perform a depreciation study which resulted in the change in the composite rate of .7%.

#### Capitalized Interest

The Authority capitalizes interest on constructed assets during the period of construction. The amount of interest cost capitalized on qualifying assets acquired with proceeds of tax exempt borrowings that are externally restricted to finance acquisition of specified assets is all interest cost of the borrowings less any interest earned on related interest-bearing investments acquired with such unexpended

proceeds from the date of the borrowings until the assets are substantially complete and are ready for their intended use. Interest cost capitalized during the years ended May 31, 2003 and 2002 was \$1,096,000 and \$1,024,000, respectively.

### **Cash and Cash Equivalents**

Investments with maturity dates of ninety days or less are considered cash equivalents.

### **Debt Service Reserve and Bond Funds**

In accordance with the 1988 General Bond Resolution, as amended (the "Resolution"), the Authority maintains a debt service reserve fund (or bond insurance, as described in Note 5) and a bond fund that is held by a 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 U.S. Treasury Notes and U.S. government securities.

### **Construction Fund**

In accordance with the Resolution, monies in the construction fund are internally designated to the costs of acquiring, constructing and replacing the water system.

### **Goodwill**

As a result of the adoption of SFAS No. 142, "Goodwill and Other Intangible Assets," effective June 1, 2002, the Authority no longer amortizes goodwill thereby eliminating an annual non-cash charge of \$150,000. In addition, the Authority was required to conduct a review for potential impairment of goodwill upon adoption and is required to perform such assessment annually. The Authority completed its review and determined that no impairment existed as of May 31, 2003.

### **Advances for Construction and Capital Reimbursement Fees**

Under current standard construction contracts with residential real estate developers and others, the developer advances to the Authority the cost of new main installations based on a flat cost per foot. Upon completion of construction, the monies are transferred to the capital reimbursement fee account. Provision exists, and is infrequently exercised, whereby the developer may receive reimbursement if the actual footage of main installed was less than 95% of the original estimate. These refunds are made from the construction advance account prior to transfer to the capital reimbursement fee account.

There exist certain construction contracts with residential real estate developers and others, whereby the developer advances the Authority the cost of new main installations based on actual costs. Upon completion of construction, the developer is either billed (not to exceed 10% of original estimate) or refunded the difference between the advance and actual cost. The monies paid by the developer are transferred from the construction advance account to the capital reimbursement fee account.

Capital reimbursement fees also include the original cost of systems paid to the Authority by municipalities and others as well as service, tapping and other fees.

During December 1998, the Governmental Accounting Standards Board issued GASB Statement No. 33, "Accounting and Financial Reporting for Nonexchange Transactions," which addresses nonexchange transactions in which a government receives value from another party without directly giving equal value in exchange. This statement causes the Authority's construction loan contracts and tapping and other fees to be recognized in the statement of revenues, expenses and changes in net assets. As a result of the adoption of this statement, the Authority has recognized \$8,647,000 of capital reimbursement fees in the statement of revenues, expenses, and changes in net assets for the current year and has restated the prior year financial statements to reflect \$12,402,000 of capital reimbursement fees recognized during the year ended May 31, 2002. These reimbursement fees are reported as a separate component of non-operating revenues and expenses since they qualify as "exchange-like" transactions under the provisions of GASB 33.

### **Customer Deposits**

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

### **Accrued Employee Welfare**

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

### **Revenues**

Revenues and expenses are distinguished between operating and non-operating items. Operating revenues generally result from providing services in connection with the Authority's principal ongoing operations. Water service revenues are recognized based on actual customer water usage, including estimates for unbilled periods. Other revenues are recognized when service has been rendered and collection is certain.

### **Use of Resources**

When both restricted and unrestricted resources are available for use, it is the Authority's policy to use unrestricted resources first, and then restricted resources as they are needed. For capital expenditures, restricted bond proceeds are used first, then other restricted resources, then unrestricted resources are used if needed.

### **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 accounting principles generally accepted in the United States of America 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 2002 balances have been reclassified in order to conform with the current year presentation.

### Recent Accounting Pronouncements

In March 2003, Governmental Accounting Standards Board issued GASB Statement No. 40, "Deposit and Investment Risk Disclosure." The deposits and investments of state and local governments are exposed to risks that have the potential to result in losses. This Statement addresses common deposit and investment risks related to credit

risk, concentration of credit risk, interest rate risk, and foreign currency risk. As an element of interest rate risk, this Statement requires certain disclosures of investments that have fair values that are highly sensitive to changes in interest rates. Deposit and investment policies related to the risks identified in this Statement also should be disclosed. The Authority does not expect adoption of this Statement, effective June 1, 2005, to have a significant impact on its disclosure pertaining to its financial position, results of operations or cash flows.

Effective June 1, 2002, the Authority adopted SFAS No. 143, "Accounting for Asset Retirement Obligations ("SFAS No. 143"). SFAS No. 143 requires an entity to record the fair value of legal obligations associated with the retirement of long-lived assets as a capitalized asset and as an asset-retirement obligation. The recognition of the depreciation of such asset and the accretion of interest on such liability will be charged to expense over the life of the assets. The adoption of this standard by the Authority did not have a significant impact on its financial position, results of operations, or cash flows for the year ended May 31, 2003.

## 2. WATER PLANT

(in thousands of dollars)

	May 31, 2002	Additions/ Reclassifications	Deletions/ Reclassifications	May 31, 2003
Land and land rights .....	\$ 18,302	\$ 762	\$ —	\$ 19,064
Distribution systems .....	650,870	38,565	(1,122)	688,313
Wells, reservoirs and structures .....	89,390	8,920	(640)	97,670
Pumping and purification equipment .....	96,437	13,357	(355)	109,439
Other .....	56,044	7,329	(1,258)	62,115
Water plant in service .....	911,043	68,933	(3,375)	976,601
Less—accumulated depreciation .....	(220,691)	(25,897)	3,295	(243,293)
Net water plant in service .....	690,352	43,036	(80)	733,308
Construction in progress .....	118,261	56,588	(68,933)	105,916
Water plant .....	\$ 808,613	\$ 99,624	\$(69,013)	\$ 839,224

Depreciation expense amounted to \$25,897,000 and \$18,265,000 for the years ended May 31, 2003 and 2002, respectively.

Water plant includes approximately \$1,104,000 of computer equipment recorded under a capital lease at May 31, 2003 and 2002.

## 3. CASH AND CASH EQUIVALENTS AND INVESTMENTS

### Cash and Cash Equivalents

Cash consists of insured (FDIC) or collateralized deposits which have carrying values of \$1,990,000 and \$4,590,000 and bank balances of \$1,964,000 and \$9,953,000 at May 31, 2003 and 2002, respectively.

### Investments

Investments consist of the following:

(in thousands of dollars)	May 31, 2003	May 31, 2002
Certificates of deposit .....	\$ 4,000	\$ 13,775
Debt service reserve and bond fund		
U.S. Treasury bills (a).....	220	64
Short-term notes (a).....	16,030	19,501
Long-term notes (a).....	6,516	5,082
Other (a).....	145	21

(continued)

(in thousands of dollars)	May 31, 2003	May 31, 2002
Construction fund		
Certificates of deposit .....	\$ 19,425	\$ 10,400
U.S. T-bills .....	76	—
Short-term notes (b) .....	15,553	19,475
Medium-term notes .....	25,114	20,613
Long-term notes (b) .....	3,377	2,163
Money Market .....	30,596	—
Other (b).....	5	125
Investment pool.....	35,675	45,207
Short-term notes .....	20,092	—
Medium-term notes .....	25,080	33,705
Long-term notes.....	2,014	—
Other .....	—	41
Investments*.....	\$203,918	\$170,172

(a) Funds are held by fiscal agent.

(b) Includes \$15,634 and \$20,210 of funds held by fiscal agent at May 31, 2003 and 2002, respectively.

\*Includes investments, construction fund, debt service reserve and bond funds.

Accrued interest on investments is included in interest and other receivables on the balance sheet. Investments bear interest rates that range from 1.05% to 6.8% and that mature at various dates through October 2022.

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.

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. Investments are reported at fair market value.

In addition, the Authority invests in an external investment pool called New York CLASS. The pool invests in obligations permissible under the Authority's investment policies. The fair value of the position of the pool is equal to the value of the pool shares.

#### 4. BONDS PAYABLE

Outstanding bonds are summarized as follows:

Series	Interest Rate	Final Maturity Date	May 31, 2002	Issued	Matured	May 31, 2003
<i>(in thousands of dollars)</i>						
<b>Water System Revenue Bonds</b>						
(a) 1993 Senior Lien .....	4.80–5.10%	2013	\$ 41,445	\$ —	\$ —	\$ 41,445
(a) 1993 Subordinate Lien.....	4.80–5.10%	2013	15,925	—	540	15,385
(a) 1994 Senior Lien .....	5.00%	2017	64,000	—	—	64,000
(a) 1994 Subordinate Lien.....	4.13–6.00%	2017	34,985	—	1,445	33,541
(a) 1997 Senior Lien .....	4.10–5.25%	2012	33,955	—	1,425	32,530
(a) 1997A Senior Lien .....	4.00–5.00%	2022	41,230	—	3,000	38,230
(b) 2001A Senior Lien .....	4.13–5.25%	2023	38,200	—	—	38,200
<b>Environmental Facilities Corporation Revenue Bonds</b>						
(b) 1998B.....	3.65–5.20%	2017	5,255	—	235	5,020
(b) 1999A .....	2.77–4.91%	2018	4,977	—	212	4,765
(b) 2000A .....	3.80–5.96%	2019	810	—	30	780
(b) 2000B.....	4.31–5.74%	2020	5,194	—	170	5,024
(b) 2001A .....	3.48–5.17%	2021	10,089	—	365	9,725
(b) 2001B.....	2.62–5.15%	2021	16,964	—	612	16,352
(b) 2002A .....	1.36–5.00%	2022	10,594	—	300	10,294
(b) 2002G.....	1.33–5.12%	2022	—	8,615	230	8,385
<b>Total bonds outstanding</b> .....			323,623	<u>\$8,615</u>	<u>\$8,564</u>	<u>323,676</u>
Less: Unamortized discount .....			4,823			4,287
Current maturities payable .....			8,408			8,440
			<u>\$310,392</u>			<u>\$310,949</u>

(a) The payment of principal and interest is insured by a municipal bond insurance policy issued by MBIA Corporation or AMBAC Indemnity Corporation.

(b) The payment of principal and interest is assured by a minimum debt service fund balance maintained by the Authority.

#### Water System Revenue Bonds

The Water System Revenue Bonds were issued to finance the cost of acquisition and construction of improvements and additions to the water system. The Water System Senior Lien Revenue Bonds are payable solely from net revenues of the Authority's water system. The Water System Subordinate Revenue Bonds are payable solely from net revenues available after payment of debt service on Senior Lien Revenue Bonds issued by the Authority.

In March 2002, the Authority defeased its remaining Series 1992B Water System Revenue Bonds in the amount of \$55,245,000 and \$17,055,000 of its remaining Series 1993 Senior Lien Water System Revenue Bonds by making a payment of \$75,328,000 to an irrevocable trust held by the Authority's fiscal agent. The transaction effectively

transferred the obligation to repay the Series 1992B and \$17,055,000 of the Series 1993 Senior Lien bonds from the Authority to the fiscal agent and therefore constituted a legal defeasance. The carrying amount of the bonds including current maturities, net of unamortized discount and issue costs of \$1,340,000 was \$70,960,000. The transaction resulted in an extraordinary loss of \$4,368,000.

In June 2003, subsequent to year end, the Authority issued \$67,395,000 of Senior Lien Bonds, Water System Revenue Bonds, Series 2003 (Refunding) to provide for the refunding, in advance of their maturities all of the \$64 million of Water System Revenue Bonds, Series 1994, dated January 1, 1994, \$2,575,000 of Water System Revenue Bonds, Series 1997, dated March 1, 1997, maturing June 1, 2004, and \$1,550,000 of Water System Revenue

Bonds, Series 1997A, dated November 1, 1997, maturing June 1, 2004. These bonds bear interest at rates ranging from 2% to 4.5% and have a final maturity date of June 1, 2017.

In July 2003, subsequent to year end, the Authority issued \$80,000,000 of Senior Lien Bonds, Water System Revenue Bonds, Series 2003C to provide for the retirement of \$45,900,000 aggregate principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2000 and \$33,200,000 aggregate principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2001. These bonds bear interest at rates ranging from 4% to 4.75% and have a final maturity date of June 1, 2026.

*Environmental Facilities Corporation Revenue Bonds*  
 (“EFC Revenue Bonds”)

The State of New York has established a State Drinking Water Program, which includes a State drinking water revolving fund (the “Revolving Fund”) to be used for purposes of the Safe Drinking Water Act. The New York State Environmental Facilities Corporation (the “Corporation”) is responsible for administering the Revolving Fund and to provide financial assistance from the Revolving Fund. The Corporation issues bonds in order to provide loans from the Revolving Fund to private water companies, political subdivisions and public benefit corporations of the State of New York. The Authority has been issued a portion of the total bond proceeds in the amounts stated in the table above to finance safe drinking water projects.

In July 2002, the Authority was issued \$8,615,000 of proceeds under the Environmental Facilities Corporation 2002G Revenue Bond Offering. The bonds have a final maturity date of October 15, 2022 and bear interest at rates ranging from 1.33% to 5.12%. The interest cost of these bonds is subsidized by the State of New York drinking water revolving fund.

In March 2002, the Authority was issued \$10,869,000 of proceeds under the Environmental Facilities Corporation 2002A Revenue Bond Offering. The bonds have a final maturity date of October 15, 2022 and bear interest at rates ranging from 1.21% to 5%. The interest cost of these bonds is subsidized by the State of New York drinking water revolving fund.

In July 2001, the Authority was issued \$17,634,000 of proceeds under the Environmental Facilities Corporation 2001B Revenue Bond offering. The bonds have a final maturity date of May 26, 2021 and bear interest at rates ranging from 2.62% to 5.15%. The interest cost of these bonds is subsidized by the State of New York drinking water revolving fund.

In July 2003, subsequent to year end, the Authority was issued \$9,130,775 of Senior Lien Bonds under the Environmental Facilities Corporation bond offering to provide for the retirement of \$100,000 principal amount of the Authority's outstanding Variable Rate Bond Anticipation

Notes, 2000, retirement of \$2,800,000 principal amount of the Authority's outstanding Variable Rate Bond Anticipation Notes, 2001, to fund a reserve account for these Senior Lien Bonds in the amount of \$913,078, and to finance additional costs of the approved projects. The bonds have a final maturity date of January 15, 2023 and bear interest at rates ranging from .721% to 4.5%. The interest cost of these bonds is subsidized by the State of New York drinking water revolving fund.

*Water System and Environmental Facilities Corporation Revenue Bonds*

Interest expense on the bonds outstanding during the fiscal year was \$15,279,000 and \$18,232,000 for the years ended May 31, 2003 and 2002, respectively.

Bond maturities payable, including mandatory sinking fund redemptions, over the next five fiscal years are as follows:

<i>(in thousands of dollars)</i>	Principal	Interest	Total
<b>Fiscal Year Ending</b>			
2003 .....	\$ 8,440	\$10,493	\$ 18,933
2004 .....	8,668	10,134	18,802
2005 .....	14,516	12,065	26,581
2006 .....	15,195	11,383	26,578
2007 .....	17,070	10,662	27,732
	<b>\$63,889</b>	<b>\$54,737</b>	<b>\$118,626</b>

**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 Water System Revenue Bonds Series 1992B–1997A plus the EFC Revenue Bonds Series 1998B–2002A or the average of the annual installments of debt service with respect to Water System Revenue Bonds Series 1992B–2001A plus the EFC Revenue Bonds Series 1998B–2002A 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 Water System Revenue Bonds Series 1992B–1997A, 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 Water System Revenue Bonds Series 2001A and EFC Revenue Bonds Series 1998B, 1999A, 2000A, 2000B, 2001A, 2001B, 2002A and 2002G Bonds, the Authority elected to maintain a minimum debt service fund balance of 10% of the proceeds.

Revenue before interest expense and depreciation and amortization was equivalent to 2.77 times (2.45 in 2002) the debt service requirement, for the year ended May 31, 2003. The minimum debt service requirement on all bonds is 1.10.

## 6. NOTES PAYABLE

Outstanding bond anticipation notes ("BANS") payable are summarized as follows:

Series	Final Maturity Date	Balance at May 31, 2002	Issued	Redeemed	Balance at May 31, 2003
<i>(in thousands of dollars)</i>					
1997	11/01/02	\$ 32,300	\$ —	\$(32,300)	\$ —
2000	05/01/05	48,100	—	(2,100)	<b>46,000</b>
2001	06/01/06	90,000	—	(1,900)	<b>88,100</b>
2003	01/01/08	—	70,000	—	<b>70,000</b>
Total notes outstanding		\$170,400	\$70,000	\$(36,300)	<b>\$204,100</b>

These notes are issued in anticipation of the issuance of long-term revenue bonds or replacement BANS, the proceeds of which will be used to repay the notes payable.

These notes are periodically remarketed, and therefore, 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 May 1, 2005, June 1, 2006, and January 1, 2008, the date of principal maturity, for the 2000, 2001 and 2003 notes, respectively.

For the years ended May 31, 2003 and 2002, the effective interest rate was .95% and 1.51%, respectively.

Interest expense on the BANS was \$2,074,000 and \$2,785,000 for the years ended May 31, 2003 and 2002, respectively.

On January 29, 2003, the Authority issued \$70,000,000 of variable rate bond anticipation notes to fund construction activities. The notes mature on January 1, 2008, and are expected to be periodically remarketed to bear interest based on the minimum interest rate that, under prevailing financial conditions, enables the notes to be sold at par, subject to the applicable effective interest rate period.

On June 27, 2001, the Authority issued \$90,000,000 of variable rate bond anticipation notes to fund construction activities. The notes mature on June 1, 2006 and are expected to be periodically remarketed to bear interest 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.

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

Tier I and II members are eligible to receive one month service credit for each year of service at retirement, with a maximum of 24 months.

Tier II, III and IV members will be able to purchase previous service credit (continuous service rules no longer apply) with member having at least two years of service to have previous service creditable.

Tier III and IV members are required by law to contribute 3% of their annual salary to the Employees' Retirement System (3% contribution ceases after ten years of membership or ten years of credited service) 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.

After five years in the retirement system, veterans will be able to purchase up to three years of military service credit, at a cost of 3% of their last year's salary, for each year of credit acquired. Member is required to have been on active duty for at least one day during the following eligible periods:

- World War 2 (12/7/41–12/31/46)
- Korean War (6/27/50–1/31/55)
- Vietnam Era (2/28/61–5/7/75)

Pension expense contractually required by New York State and recorded in the Authority's accounts was \$1,853,000 and \$31,000 for the years ended May 31, 2003 and 2002, respectively. The Authority has recorded an accrued retirement contribution 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 obligation 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 \$13,749,000 and \$12,548,000 at May 31, 2003 and 2002, respectively.

## 9. POSTRETIREMENT BENEFITS

The Authority's employees participate in the New York State Health Insurance Plan, 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 \$1,691,000 and \$1,385,000 for the years ended May 31, 2003 and 2002, respectively.

## 10. CAPITAL LEASES

In June 2000, the Authority entered into a capital lease agreement for computer equipment. Future minimum payments under the capital lease obligation are scheduled as follows:

Year Ending May 31, (in thousands of dollars)	
2004 .....	\$217
2005 .....	216
2006 .....	216
Total minimum lease payments .....	649
Less: amounts representing interest.....	31
Present value of minimum lease payments.....	618
Less: current portion.....	193
	<b>\$425</b>

## 11. COMMITMENTS AND CONTINGENCIES

### Operating Leases

As of May 31, 2003, the Authority is obligated under several operating leases with various lease terms through 2008, for meter reading, telephone and computer equipment:

Year Ending May 31, (in thousands of dollars)	
2004 .....	\$295
2005 .....	290
2006 .....	68
2007 .....	59
2008 .....	49
	<b>\$761</b>

Rental expense for operating leases was \$276,000 for the years ended May 31, 2003 and 2002.

### Legal Proceedings

The Authority is involved in various litigation resulting from the ordinary course of business. In the opinion of management, and based on advice of legal counsel, the ultimate liability, if any, to the Authority will not have a material effect on the Authority's financial position, revenues invested in facilities or cash flows.

## Report of Independent Auditors

To the Members of Suffolk County Water Authority

In our opinion, the accompanying balance sheets and the related statements of revenues, expenses and changes in net assets and of cash flows present fairly, in all material respects, the financial position of Suffolk County Water Authority (the "Authority") at May 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. 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 auditing standards generally accepted in the United States of America 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.

As more fully discussed in Note 1, the Authority restated its financial statements for the year ended May 31, 2002 as a result of adoption of Governmental Accounting Standards Board Statements No. 33 and 34.

The Management's Discussion and Analysis and the supplementary information on pages 6 through 9 is not a required part of the basic financial statements but supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consist principally of inquiries of management regarding the presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

July 25, 2003

*Priscilla Waterhouse Coopers LLP*

## Regional Offices and Communities Served

**Western Regional Office:** Regional Manager **Clifford Foy** • 260 Motor Parkway, Hauppauge, NY 11788

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

**Central Regional Office:** Director of Customer Service **Steven Romano** • 2045 Route 112, Suite 1, Coram, NY 11727

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

**Eastern Regional Office:** Regional Manager **Dona Roberts** • 624 Old Riverhead Road, Westhampton Beach, NY 11978

Amagansett	East Yaphank	Montauk	Quogue	Village of Southampton
Bridgehampton	Flanders	Moriches	Remsenburg	Village of Westhampton Dunes
Calvertont†	Fleets Neck	New Suffolk	Riverside	Wainscott
Camp Hero	Greenport†	North Haven	Rose Grove	Watermill
Center Moriches	Laurel	North Sea	Sag Harbor	Westhampton
Cutchogue	Manorville	North Shirley	Sagaponack	Westhampton Beach
East Hampton	Mastic	Noyack	Shinnecock Hills	
East Marion	Mastic Beach	Oakville	Shirley	
East Moriches	Mattituck	Orient	Southampton	*Included in Wholesale Water District
Eastport	Mattituck Creek East	Peconic	Southold	†Serves portion of area
East Quogue	Mattituck Creek West	Quogue	Speonk	



**Authority Members** (from left to right):  
 John E. Gee, Jr., Eric J. Russo, Esq., George Proios,  
 Michael A. LoGrande and Melvin M. Fritz, D.O., M.D.

**Authority Members**

- Michael A. LoGrande  
*Chairman*
- Melvin M. Fritz, D.O., M.D.
- John E. Gee, Jr.
- Eric J. Russo, Esq.
- George Proios  
*Secretary*

- Steven T. Burns, P. E.  
*Director of Distribution*
- Larry B. Kulick, C.P.A.  
*Director of Finance*
- Michael A. Litka  
*Director of Information Technology*
- Robert L. Murray  
*Director of Production Control*

**Management Staff**

- Stephen M. Jones  
*Chief Executive Officer*
- Nicolo DiBartolo  
*Chief Financial Officer*
- Michael R. Frank  
*Deputy Chief Executive Officer for Customer Service*
- Herman J. Miller, P. E.  
*Deputy Chief Executive Officer for Operations*
- Michael Stevenson  
*Deputy Chief Executive Officer for Administration*
- Timothy J. Hopkins, Esq.  
*General Counsel*

- Joseph M. Pokorny, P. E.  
*Chief Engineer*
- Karen A. Randazzo  
*Director of Laboratory Services*
- Steven Romano  
*Director of Customer Service*

**Consultants**

- United States Trust Company of New York  
*Bond Trustee*
- PricewaterhouseCoopers LLP  
*Independent Accountants*
- Citigroup Global Markets Inc.  
*Financial Consultant*
- Nixon Peabody  
*Bond Counsel*
- Leggette, Brashears & Graham, Inc.  
*Consulting Groundwater Geologists*



**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 1998. This is a renewable designation, and the team 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 Groundwater Guardian designation enables this area to join with Groundwater Guardian communities throughout North America in a unified effort to motivate people to learn more about groundwater and help protect this essential resource.



**LEGEND**

- SCWA Service Areas
- SCWA Non-Service Areas



**Administration Office**  
**4060 Sunrise Highway • Oakdale, NY 11769**  
**(631) 589-5200**