

*Going to new heights to bring home
our most natural resource*



**Erie County Water Authority
2001 Annual Report**

A Message from the Commissioners

Respectfully submitted to the:

*Honorable George E. Pataki
Governor of the State of New York*

*Honorable Carl H. McCall
Comptroller of the State of New York*

*Honorable Joel A. Giambra
County Executive of Erie County*

*Honorable Albert DeBenedetti
Chairman, Erie County Legislature*

*Honorable Ronald B. Stafford
Chairman, Senate Finance Committee*

*Honorable Herman D. Farrell
Chairman, Assembly Ways and Means
Committee*

*Honorable Members of the New York State
Legislature*

*Honorable Members of the Erie County
Legislature*

The Erie County Water Authority is an independent, public benefit corporation created in 1949 by a special act of the New York State Legislature known as Title III Article V of the Public Authorities Law.

The Authority is not an agency of New York State and is totally independent of Erie County government. It operates as a self-sustaining business enterprise and pays all operating expenses out of revenues generated from the sale of safe, clean water to its customers. All revenues received must be used for operating expenses, capital improvements and paying outstanding debts.

The Authority has been operating for 48 years solely for the benefit of our customers that rely on our product everyday, 24 hours a day, 365 days a year.

It is in celebration of the Authority's successful efforts in producing and reliably delivering high quality, affordable water throughout Western New York, and our contributions to the quality of life in the region, that the Board of Commissioners submits the 48th Annual Report of the Erie County Water Authority.



Board of Commissioners: Robert J. Lichtenthal Jr., Mark G. Patton, Acea Mosey-Pawłowski – (from left to right)

The Chairman's Message

Water issues have ascended to the forefront of the regional agenda in Western New York; a reminder of the significant contributions safe, clean water makes on our everyday lives. Never has this fact been more evident than since the tragic events of September 11, and the threats to the nation's public water systems that followed.

For 48 years, the Erie County Water Authority has enhanced the quality of life throughout Western New York by supplying customers an abundant supply of high-quality, affordable drinking water.

Under the direction of the current Board of Commissioners and senior management team, the Authority has evolved into an efficiently run business enterprise. This evolution has greatly benefited our customers, and is the result of the hard work and dedication of every single Authority employee.

Our employees have made the Authority one of the top water utilities in the country. This industry leadership assures that our customers receive professional, cost-effective service everyday, 365 days a year.

As the water industry becomes more regulated and competitive, the Authority is focused on the future and is well positioned to meet the challenges that lie ahead.

Thank you for your continued support, and I look forward to serving our customers for another year as Chairman of the Board of Commissioners.

Sincerely,

Mark G. Patton
Chairman



Promoting Regionalism

The Authority continued its efforts to foster relationships with local municipalities to assist them in their quest to provide water more efficiently and affordably, on behalf of their residents.

The Municipal Liaison led the effort by working with state, county, local government officials, and their land use and engineering personnel, to develop strategies concerning Western New York's current and future water supply needs.

The Authority also continued its participation on the Southern Tier West Regional Planning Board Technology Committee, which deals with Geographic Information Systems (GIS) and commerce issues. The Authority distributes its GIS mapping data to municipalities to help plan for water infrastructure needs.

In cooperation with local governments, the Authority also coordinated the planning, design and construction of several water supply and distribution projects; including the replacement of waterlines in the Towns of Amherst, Lancaster and West Seneca, and the construction of new lines to service residential and commercial developments in Amherst, Clarence, Hamburg, Orchard Park, Cheektowaga and Lancaster.

The Authority, in conjunction with the Monroe County Water Authority, also completed work on the Genesee County Public Water Supply program and will begin supplying water to western Genesee County in late 2002.



United States Congressman Jack Quinn presents a \$1.35 million check to the Board of Commissioners, Erie County Executive Joel Giambra and City of Buffalo Public Works Commissioner Joseph Giambra for infrastructure improvements in the City of Buffalo.



Crews work on a 54-inch main break behind the Authority's Ball Pump Station in the Town of Amherst. The break was one of the largest in the Authority's history and was repaired without any interruption in service.

System Maintenance

The Distribution Department is responsible for maintaining the Authority's extensive distribution system, which includes 2,173 miles of pipeline, 14,308 hydrants, 21,940 valves and numerous appurtenances. The Authority's system-wide preventive maintenance program has continued to improve the reliability of the system and work productivity.

Last year, line maintenance crews completed 1,346 waterline, valve and hydrant repairs and performed 11,276 work orders.

Authority mechanics efficiently handled 1,372 preventive maintenance orders and repairs to the Authority fleet of 130 vehicles and construction equipment.

The meter shop continued to install remote read meters that can be read with a hand held computer from outside a home or business. Currently, the Authority has 136,967 residential and commercial meters and 740 large commercial meters in service. More than 60 percent of residential meters have been changed to remote read, and 80 percent of large commercial meters have been changed to more accurate, current production meters.

The remote meter reading program has reduced the hours needed to determine service volume and has resulted in greater customer satisfaction.

Putting Customers First

In addition to providing safe, high-quality water at one of the lowest rates in the state, the Authority also reaches out to its customers to provide them important information about the services it offers.

Customer service representatives are well trained to handle both billing and service calls, resulting in informed and prompt responses to customer inquiries. Last year, Authority representatives handled 73,186 calls, processed 39,331 work orders and serviced 2,246 walk-in customers.

Customer service representatives are also responsible for preparing and mailing bills and postcards for meter readings for more than 136,478 active accounts. Last year, the Authority distributed 1,023,758 water bills and read-by-mail postcards. This number was significantly higher than the previous year due to an increase in the Authority's customer base. In addition, Customer Service processes all payments and administers collection procedures. The Authority's collection rate was 99.7 percent last year. This rate is one of the highest collection rates of any local utility.

The Authority also continued its efforts to educate customers about its operations and water quality issues.

The Public Affairs office mailed thousands of information brochures, conducted plant tours and responded to inquiries from students, teachers, customers, public officials, civic organizations and the media.

Public Affairs also participated in several community events, managed the Authority's first-ever telephone customer survey and prepared public service messages for local radio and television programs.



Senior Water Treatment Plant Operator John Rodish explains the Authority's SCADA system to students from the University at Buffalo during a tour of the Van de Water Treatment Plant.



Dependable Service

The Production Department operates and maintains the Authority's two water treatment plants, 24 pumping stations and 34 water storage tanks. Last year, the Authority produced and delivered a record 25.5 billion gallons of water.

The Production Department continued to pursue technologically advanced methods to manage the system with increased efficiency and improved service.

The Van de Water Treatment Plant began its first year under the control of the Supervisory Control and Data Acquisition System (SCADA). This computer-based system constantly monitors all pumping stations and storage tanks through microwave communication and computer analysis. SCADA has become vitally important to the Authority's system efficiencies and has significantly improved operational control.

The Authority also continued its staged replacement of filter media at the Sturgeon Point Treatment Plant. Four new filters were installed and now six out of ten filters have been replaced.

Last year, the Authority again displayed its commitment to the environment by moving 6,400 cubic yards of filter plant residuals to a brownfields site in Chautauqua County. The Authority was granted a beneficial use determination by the Department of Environmental Conservation. Residuals will be used for topsoil blending and turf farming.

Production also installed emergency shut off valves in the chlorine storage tank rooms at the Authority's two treatment facilities. In the event a leak is detected, the valve will shut the tank off immediately and prevent harmful gases from escaping into the environment.

In response to the events of September 11, and the threats to our nation's water systems that followed, the Authority accelerated its security program. Improved measures were completed ahead of schedule at all facilities throughout the system. The Authority remains in a heightened state of alert and will continue to work diligently to protect our region's water supply.

Safety and Professional Development

The Authority is committed to providing its employees a safe and rewarding work environment.

The Human Resources Department has a full-time Training and Safety Officer that oversees the Authority's training and safety programs and makes sure that all federal and state regulations are met.

For the seventh consecutive year, employees completed more than 4,000 hours of safety training in areas such as hazardous material handling, backhoe safety, heavy equipment operation and work site safety.

Last year, employees continued to participate in educational training, licensing programs, and professional associations to stay ahead of the latest industry trends and develop their skills to the highest possible levels.

Employees also are afforded the opportunity to register for college courses and/or degree programs related to their employment duties. Upon the successful completion of their training or coursework, employees are eligible for partial or full expense reimbursement from the Authority.

The Authority's proactive safety and educational training programs have significantly benefited customers through reduced operating costs and improved employee performance.

Supporting Efficient Operations

The Administration Department continued to concentrate on developing and managing the Authority's purchasing, storage systems and information services.

The purchasing system was improved with a revised policy and several electronic system enhancements that have improved order tracking and payment releases to vendors. Last year, the Authority produced 7,839 purchase orders totaling \$30,234,455 in procurements and payments. The new document-imaging program processed and archived all Authority purchases. The program identifies all aspects of the procurement from its original requisition to the final payment. Contracts used to acquire the purchase agreements, specification sheets, detail sheets, warranties and maintenance are all optically available in the enhanced purchasing system.

Continuing its effort toward shared purchasing, the Authority used New York State or Erie County contracts for more than 1,700 purchases in 2001. This cost-effective, bulk-purchasing process has resulted in substantial savings for the Authority.

The Administration Department also managed the Authority's physical inventory of \$1.3 million of materials and supplies. This was a 6.17 percent increase from the previous year and was due to the Authority's expanding service area.

Information Services serves as the primary administrative support for all Authority operations. Last year, the department completed 24,276 work orders. It also manages all Authority file and retrieval processes, office supplies, secretarial services, new service applications, mail and general office operations.

Water You Can Feel Good About

The Water Quality Department maintains a highly trained staff and uses state of the art technology to assure that Authority customers receive water that is safe, clean and pure.

Last year, the Authority conducted more than 70,000 tests for roughly 200 contaminants. All tests met or exceeded the most stringent government regulations mandated by the Environmental Protection Agency and the New York State Department of Health.

After extensive research, Water Quality implemented several changes and additions to the Quality Assurance/Quality Control Program of the bacteriology laboratory in order to satisfy the requirements of the National Environmental Laboratory Accreditation Program (NELAP) and the State's Environmental Laboratory Approval Program (ELAP). The Authority's water quality lab is one of only a few water quality labs in New York State to be accredited by both organizations.

The Authority also obtained first time certification to test non-potable water for total and fecal coliform bacteria.

In response to the tragic events of September 11, and the bioterrorism threats that followed, the Authority doubled its sampling throughout its distribution system to rule out the presence of biological agents. No biological agents were detected.

As an additional safety measure, the Authority began using the MicroTox Testing System. This state of the art system allows the Authority to monitor the toxicity levels of its source, distribution and stored water. In the event of an accidental or deliberate chemical contamination of the Authority's water supply, the MicroTox can provide early warning signals and allow for rapid response to the problem.

Water Quality's Laboratory Information Management System (LIMS) began to be fully utilized to generate all lab data on microscopic organisms, chlorine decay pattern and Heterotrophic Plate Count (HPC) in the distribution system. The LIMS system has drastically improved the Authority's collection and reporting capabilities.



Improving Efficiency

The Engineering Department plays a vital role in the Authority's ability to provide high quality water and efficient service to an expanding customer base.

Engineering is responsible for the study, design and construction of major capital improvements to the Authority's distribution system. The department also manages the Authority's Geographical Information System (GIS) and all restoration work.

Last year, Engineering supervised the design and construction of 18,650 linear feet of pipeline throughout the Authority's service district, including the City of Lackawanna and the towns of Cheektowaga, Amherst and Newstead. The total cost for these projects was \$3.2 million. The Authority also replaced ten 16-inch valves with new 24-inch valves at eight locations in the Towns of Cheektowaga, West Seneca, Hamburg and Amherst; completed a \$1 million tank refurbishing project on the Cole Road, Eden III and Eden IV storage tanks; and installed 1,281 small and large service connections.

The Authority's continuous facility maintenance and capital investment programs will increase the life and efficiency of its system and save customers from more costly improvements in the future.

Commentary from the Executive Director

2001 was another successful and progressive year at the Authority as we continued to improve efficiencies and reduce operating costs on behalf of our customers.

Much of the Authority's efficient operations can be attributed to our financial commitment to infrastructure improvements over the last five years. During this period, the Authority has invested more than \$65 million in system upgrades that have significantly improved service delivery. Due to this investment, our system will reliably meet the demands of an increasing customer base resulting from our sustained efforts to regionalize Western New York's public water systems.

Last year, we assisted several local governments in their attempts to provide water more cost-effectively. Following three years of talks and a significant financial commitment from the Authority, the City of Tonawanda has decided to merge its system with the Authority. The merger will result in 6,000 new customers and increased revenues for the Authority, and significant savings for Tonawanda's ratepayers.

In cooperation with the County of Erie, the Authority also helped fund a design study for the Southtowns Water Consortium that will determine the feasibility of supplying public water to seventeen communities in southern Erie County.

As a result of the positive impact the consolidation of public water systems has had on our community, the Authority will continue to pursue regional opportunities that will achieve our mission of providing safe, high quality water at an affordable rate.

It is an exciting time to be a part of the Authority, and we look forward to your continued support.

Sincerely,

Robert A. Mendez



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Report of Independent Accountants

To the Members of the
Erie County Water Authority

In our opinion, the accompanying balance sheets and the related statements of net income and earnings reinvested in the business and cash flows present fairly, in all material respects, the financial position of the Erie County Water Authority (the Authority) at December 31, 2001 and 2000, and the results of their operations and their 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 misstatements. 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 our opinion.

PricewaterhouseCoopers LLP
March 15, 2002

ERIE COUNTY WATER AUTHORITY

Balance Sheet

	December 31,	
	<u>2001</u>	<u>2000</u>
Assets		
Water plant, net	\$ 256,408,116	\$ 256,040,594
Invested reserve funds		
Future construction	3,925,943	3,905,792
Debt service reserve fund	5,696,514	5,759,357
Net increase in the fair market value of investments	<u>3,683</u>	<u>105,097</u>
	<u>266,034,256</u>	<u>265,810,840</u>
Current Assets:		
Cash and cash equivalents	19,199,952	15,047,157
Customers' accounts receivable, less allowance for doubtful accounts of \$273,046 and \$289,173, respectively	4,363,929	3,811,011
Debt service fund (at amortized cost)	4,142,336	4,878,389
Investments	3,050,000	4,992,310
Interest receivable and other assets	1,486,250	2,121,801
Materials and supplies	<u>1,859,323</u>	<u>1,440,941</u>
Total current assets	<u>34,101,790</u>	<u>32,291,609</u>
Unamortized bond discount and expense	1,585,304	1,777,742
Long-term investment	<u>8,154,128</u>	<u>8,673,074</u>
Total assets	<u>\$ 309,875,478</u>	<u>\$ 308,553,265</u>
Capitalization and Liabilities		
Capitalization:		
Earnings reinvested in the business	\$ 168,492,470	\$ 163,638,247
Contributions in aid of construction	<u>37,899,067</u>	<u>36,859,748</u>
Total capitalization	<u>206,391,537</u>	<u>200,497,995</u>
Water revenue bonds - long term	<u>83,607,830</u>	<u>87,333,747</u>
Total capitalization and long term debt	<u>289,999,367</u>	<u>287,831,742</u>
Current liabilities:		
Accounts payable	4,473,066	4,341,286
Water revenue bonds - current	3,725,917	3,910,472
Interest and other accrued liabilities	4,221,299	3,806,941
Accrued retirement contributions	1,980,492	2,074,072
Construction retention	<u>239,384</u>	<u>308,349</u>
Total current liabilities	<u>14,640,158</u>	<u>14,441,120</u>
Accrued sick pay	1,527,878	1,431,705
Long-term interest payable	3,499,125	4,531,023
Advances for construction	<u>208,950</u>	<u>317,675</u>
Total capitalization and liabilities	<u>\$ 309,875,478</u>	<u>\$ 308,553,265</u>

The accompanying notes are an integral part of these financial statements

ERIE COUNTY WATER AUTHORITY

Statement of Net Income and Earnings Reinvested in the Business

	Year ended December 31,	
	<u>2001</u>	<u>2000</u>
Operating revenues	\$ 45,633,628	\$ 43,013,977
Operating expenses:		
Operation and administration	22,397,889	19,911,620
Maintenance	6,494,451	5,849,456
Depreciation and amortization	<u>9,061,901</u>	<u>8,793,168</u>
Total operating expenses	<u>37,954,241</u>	<u>34,554,244</u>
Operating income before miscellaneous income and net interest charges	7,679,387	8,459,733
Net interest charges:		
Interest expense	4,911,337	5,327,781
Interest income	(2,054,934)	(2,886,249)
Amortization of investment premium/discount	8,170	-
Interest capitalization during construction	<u>(39,409)</u>	<u>(18,299)</u>
Net interest charges	<u>2,825,164</u>	<u>2,423,233</u>
Net income	<u>\$ 4,854,223</u>	<u>\$ 6,036,500</u>
Earnings reinvested in the business:		
Beginning of year	<u>163,638,247</u>	<u>157,601,747</u>
End of year	<u>\$ 168,492,470</u>	<u>\$ 163,638,247</u>

The accompanying notes are an integral part of these financial statements

ERIE COUNTY WATER AUTHORITY

Statement of Cash Flows

	Year ended December 31,	
	<u>2001</u>	<u>2000</u>
Cash flows from operating activities:		
Net income	\$ 4,854,223	\$ 6,036,500
Adjustments to reconcile net income to net cash provided by (used for) operating activities -		
Depreciation and amortization	9,061,901	8,793,168
Interest expense, net	36,612	(715,983)
Interest capitalization during construction	(39,409)	(18,299)
Change in:		
Debt service fund	736,053	(1,077,900)
Customers' accounts receivable	(552,918)	58,027
Materials and supplies	(418,382)	31,724
Other assets	578,834	(2,601,219)
Accounts payable	131,780	1,727,825
Accrued retirement contributions	(93,580)	9,059
Construction retention	(68,965)	(75,022)
Other liabilities	(1,335,273)	165,119
Sick pay accrual	96,173	44,147
	<u>12,987,049</u>	<u>12,377,146</u>
Net cash provided by (used for) operating activities		
Cash flows from investing activities:		
Proceeds from the sale or maturity of investments	65,277,879	102,596,062
Purchase of investments	(62,198,414)	(106,378,457)
Net decrease (increase) in the fair value of investments	101,414	(89,336)
Cash transfer for investment	105,604	(99,890)
Additions to water plant, net of disposals	<u>(9,140,859)</u>	<u>(7,784,767)</u>
	<u>(5,854,376)</u>	<u>(11,756,388)</u>
Net cash provided by (used for) investing activities		
Cash flows from capital and related financing activities:		
Repayment of water revenue bonds	(3,910,472)	(7,503,414)
Increase in contributions in aid of construction	1,039,319	1,146,918
Increase (decrease) in advances for construction	<u>(108,725)</u>	<u>152,060</u>
	<u>(2,979,878)</u>	<u>(6,204,436)</u>
Net cash provided by (used for) capital and related financing activities		
Net increase (decrease) in cash and cash equivalents	4,152,795	(5,583,678)
Cash and cash equivalents:		
Beginning of year	<u>15,047,157</u>	<u>20,630,835</u>
End of year	<u>\$ 19,199,952</u>	<u>\$ 15,047,157</u>

The accompanying notes are an integral part of these financial statements

ERIE COUNTY WATER AUTHORITY

Notes to Financial Statements

1. Organization and significant accounting policies

Organization and summary of operations

The Erie County Water Authority (the Authority) is a public benefit corporation created in 1949 by the State of New York. 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 or those of any other state or federal regulatory agency. The rates established by the Authority do not require PSC approval.

The Erie County Water Authority operates its business activities on a direct service basis where the Authority owns the assets and is responsible for their operation, maintenance, improvement and replacement; on a leased managed service basis where the Authority leases the assets and is responsible for the operation and maintenance of the assets while the lessor is responsible for the improvement and replacement of assets; and on a bulk sales basis where the Authority contracts with the customer to provide water while the customer owns the assets and is responsible for their operation, maintenance, improvement and replacement as well as billings and customer collections.

The Authority began with a mandate to provide potable water to all locations within Erie County, except Buffalo, Tonawanda and Grand Island, and has fulfilled this mandate by providing water to over 540,000 residents of Erie County operating on one of the three bases set forth above - direct service, leased managed service or bulk service. The Authority has had a regional outlook for many years as evidenced by our service expansion throughout the county and by the Inter-Community Transmission main built in the early 1990's to expand water service to the Cattaraugus Indian Reservation and some Chautauqua County customers. During fiscal year 2000 the Authority converted the Village of Depew and the Town of Clarence from bulk service to direct service and added over ten thousand direct service customers to its operations and asset base. The Authority has also agreed to provide water to residents of Western Genesee County in a shared venture with the Monroe County Water Authority and the State of New York. In addition, the Authority is under agreement to provide direct service to the City of Tonawanda in 2003.

Basis of accounting

The Authority prepares its financial statements using the accrual basis of accounting. The activities of the Authority are reported in conformity with governmental accounting and financial reporting principles of the Governmental Accounting Standards Board (GASB). As allowed by governmental accounting standards, the Authority has elected not to apply Financial Accounting Standards Board pronouncements issued after November 30, 1989.

Reclassification

Certain prior year amounts have been reclassified to conform with the current year presentation.

Water plant

The cost of additions to water plant including purchased or contributed property and replacements of retired units of property is capitalized. Cost includes direct material, labor, overhead and an allowance for funds used during construction equivalent to the cost of borrowed funds used for construction purposes. Overhead is added proportionately to the cost of a project on a monthly basis. The cost of retirements of water plant is charged against accumulated depreciation. Maintenance and repairs are charged to expense as incurred, and major betterments are capitalized.

Depreciation of water plant is computed using the straight-line method based upon annual rates established in accordance with PSC guidelines, which range from 1% to 20%.

Depreciation expense approximated 2.3% and 2.4% of the original cost of average depreciable property for the years ended December 31, 2001 and 2000.

Investment securities

Investments are carried at market value based on quoted market prices for those investments subject to market forces and at amortized cost for investments not subject to market forces. The cost of investments sold is determined using the specific identification method and then adjusted to market value changes to reflect the combined net change in these elements in the income statement.

The Authority's deposits at December 31, 2001 were entirely covered by federal deposit insurance or by collateral held by the Authority's custodial banks in the Authority's name.

Materials and supplies

Materials and supplies are stated at the lower of cost or market, cost being determined on the basis of moving-average cost.

Accrued sick pay

Certain Authority employees who enter retirement, or who are separated from employment other than for cause, are paid 80% of their earned and unused sick leave pursuant to collective bargaining agreements and board policy. Sick pay is accrued when earned.

Unamortized bond discount and expense

Bond discount and expense resulting from the issuance of water revenue bonds have been deferred and are being amortized over the life of the bonds using the straight-line method.

Long-term investment

The long-term investment is accounted for at cost plus accrued income. See further discussion at Note 8.

Advances for construction and contributions in aid of construction

Advances for construction primarily represent amounts received from contractors for water main extensions. Upon completion of the extension, the remaining advance is transferred to contributions in aid of construction.

Contributions in aid of construction represent amounts received from individuals, governmental agencies, and others, to reimburse the Authority for construction costs incurred on capital projects or the original cost of water plant systems contributed to the Authority by municipalities and others. During 2000, the Authority recorded asset values and contributions in aid of construction from the Village of Depew and the Town of Clarence in excess of \$11,036,000 and assumed responsibility for the operation, maintenance and improvements to these water systems now and in the future.

Operating revenues

Operating revenues are recorded as water service is supplied. Water supplied, but not billed, as of

the calendar year-end is estimated based upon historical usage and has been accounted for as earned but unbilled revenue. Billings in advance of water supplied are accounted for as a reduction to earned but unbilled revenue.

Statement of cash flows

For purposes of the statement of cash flows, the Authority considers cash and cash equivalents to be all unrestricted cash accounts and short-term investments purchased with an original maturity of generally three months or less. Cash paid for interest on the water revenue bonds amounted to \$6,077,179 for 2001 versus \$5,790,082 for 2000 (consisting of \$4,591,771 current interest and \$1,198,311 related to the partial defeasance of the 1992 and 1993 Capital Appreciation Bonds).

Income taxes

As a public benefit corporation, the Authority is exempt from Federal and State income taxes.

2. Water plant

	December 31,	
	2001	2000
	(in thousands)	
Buildings and structures	\$ 166,620	\$ 164,675
Mains and hydrants	151,518	146,588
Equipment	26,937	25,465
Land	2,194	2,194
Other	<u>37,272</u>	<u>35,861</u>
Water plant in service	384,541	374,783
Less accumulated depreciation	<u>130,836</u>	<u>122,751</u>
	253,705	252,032
Construction work in progress	<u>2,703</u>	<u>4,009</u>
	<u>\$ 256,408</u>	<u>\$ 256,041</u>

3. Water revenue bonds

Water revenue bonds are summarized as follows:

<u>Series</u>	<u>Final annual installment payment due</u>	<u>Year of earliest redemption</u>	<u>Interest rate</u>	<u>Original issue</u>	Balance as of	
					2001	2000
					(in thousands)	
Series 1992FR	12/01/08	2006	6.20-6.30%	\$ 50,270	\$ 4,473	\$ 4,473
Series 1993A	12/01/16	2009	Variable (*)	27,500	27,500	27,500
Series 1993B	12/01/16	2009	Variable (*)	15,000	15,000	15,000
Series 1993FR	12/01/05	1997	4.88-6.17%	43,886	18,206	21,181
Series 1998B	12/15/17	1998	3.65-5.20%**	7,781	6,525	6,835
Series 1998D	10/15/19	2000	3.90-5.15%**	16,860	<u>15,630</u>	<u>16,255</u>
					<u>\$ 87,334</u>	<u>\$ 91,244</u>
Less portion due within one year					<u>3,726</u>	<u>3,910</u>
					<u>\$ 83,608</u>	<u>\$ 87,334</u>

(*) The interest rate was 1.40% and 4.55% at December 31, 2001 and 2000, respectively.
 (**) Gross rates subject to subsidy from the New York State Environmental Facilities Corporation (EFC).
 FR Fourth Resolution

The Series 1992 Bonds represent Capital Appreciation Serial Bonds (Appreciation Bonds), the Series 1993A and Series 1993B Bonds represent Variable Weekly Bonds and the Series 1993 Fourth Resolution Bonds represent Current Interest Bonds and Appreciation Bonds. Interest on the Current Interest Bonds and Variable Weekly Bonds is payable semi-annually on June 1 and December 1. Interest on the Appreciation Bonds is compounded semi-annually on June 1 and December 1 but is not payable until bond maturity. The accrued interest on the Appreciation Bonds is reflected as current and long-term interest payable.

Concurrent with the issuance of the Series 1993A Bonds and the Series 1993B Bonds, the Authority entered into interest rate swap agreements as a hedge against fluctuating interest rates. The forward interest rate swap agreement for the Series 1993B Bonds became effective in March 1996. The interest rate swap agreements provide for the Authority and a counterparty to exchange a net dollar amount calculated as the difference between a weekly variable rate and a contractual fixed rate of 5.24% and 5.89%, for the Series 1993A Bonds and the Series 1993B Bonds, respectively. Settlement with the counterparty occurs with the semi-annual payment of interest on May 31 and November 30. Amounts receivable or payable are accrued as a component of interest expense. The notional amount of the interest rate swap agreement is consistent with the Series 1993A Bond and Series 1993B Bond issuance amounts and decreases concurrent with subsequent maturities of the Series 1993A Bonds and Series 1993B Bonds.

The Current Interest Serial 1998B and 1998D Series Bonds were issued to the EFC under their aggregate pool financings identified as New York State Environmental Facilities Corporation State Water Pollution Control Revolving Fund Revenue Bond Series 1998B (EFC Project No. 15568) and Bond Series 1998D (EFC Project No. 16504) in 1998. The 1998B and 1998D bonds in the amounts of \$7,780,931 and \$16,859,700, respectively, representing the Authority's portion of these financings, were issued to cover the costs of the construction of two new clearwell water tanks and a new pumping station at the Authority's Sturgeon Point plant. Payments are made to the bondholders as follows:

	<u>Interest</u>	<u>Principal</u>
1998B	June 15 and December 15	December 15
1998D	April 15 and October 15	October 15

The bonds bear a variable rate of interest from 3.65% to 5.20% over their respective installment payment dates ending on December 15, 2017 and October 15, 2019, respectively. The terms of the borrowings provide for an interest subsidy of approximately one-third of the stated interest rates shown above. The subsidy is generated from a United States Environmental Protection Agency grant to the EFC which EFC invests and credit the borrower with the earnings on the invested funds as an offset to the interest payable on the bonds.

Total principal and interest payments relating to Water Revenue Bonds for the next five years are

summarized as follows:

Year ending December 31,	Principal	CAB Interest	Current Interest	Total
2002	\$ 3,725,917	\$ 1,959,083	\$ 4,305,251	\$ 9,990,251
2003	5,805,000	-	4,196,668	10,001,668
2004	5,955,000	-	3,869,494	9,824,494
2005	6,740,000	-	3,522,976	10,262,976
2006	3,238,577	2,996,423	3,215,281	9,450,281
2007-2019	<u>61,869,253</u>	<u>3,635,747</u>	<u>21,989,821</u>	<u>87,494,821</u>
	\$ 87,333,747	\$ 8,591,253	\$ 41,099,491	\$ 137,024,491
Less portion due within one year	<u>3,725,917</u>	<u>1,959,083</u>	<u>4,305,251</u>	<u>9,990,251</u>
	<u>\$ 83,607,830</u>	<u>\$ 6,632,170</u>	<u>\$ 36,794,240</u>	<u>\$ 127,034,240</u>

As provided by the respective bond resolutions, the Series 1993A Bonds and the Series 1993B Bonds are redeemable prior to maturity at the election of the Authority, at any time. In order to redeem these bonds the Authority would be required to unwind the swap agreements.

Prior to 1993, the Authority completed a plan of restructuring a significant portion of its debt through a series of bond issuances. The net proceeds from these issuances and certain existing funds were deposited with an escrow agent pursuant to refunding agreements, and invested in U.S. Government securities. The maturities of these invested funds and related earnings thereon are expected to provide sufficient cash flow to meet the debt service requirements of the defeased bonds as they mature. These advance refunding transactions effectively released the Authority from its obligation to repay these bonds and constituted in-substance defeasances. The principal outstanding on the bonds defeased prior to 1993 is \$70,447,330 at December 31, 2001 with maturities ranging from the year 2002 to the year 2014.

Beginning in 1998, the Authority has significantly reduced its debt. On December 1, 1998, the Authority paid \$7,701,125 to discharge principal and accrued interest on the Series 1992 Bond Issue due December 1, 2017.

In November 1999, the Authority defeased a portion of the 1993 Fourth Resolution Taxable Bonds. Available cash of \$13,684,547 was deposited with an escrow agent pursuant to an escrow agreement, and invested in U.S. Government securities. The maturities of these securities and related earnings thereon are expected to provide sufficient cash flow to meet the debt service requirements of the defeased portion of the 1993 Fourth Resolution Taxable Bonds as they mature. This transaction effectively released the Authority from its obligation to repay the defeased portion of the Series 1993 Fourth Resolution Bonds and constituted an in-substance defeasance. This transaction resulted in a difference of \$19,422 between cash put into escrow and the net carrying amount of the debt. This difference has been deferred and will be amortized as a component of interest expense over the remaining life of the debt. The principal outstanding is \$9,369,880 at December 31, 2001 with maturities ranging from the year 2002 to the year 2005.

In December 2000, the Authority defeased a portion of the 1992 Fourth Resolution Bonds and a portion of the 1993 Fourth Resolution Taxable Bonds. Securities and available cash of \$4,191,215

was deposited with an escrow agent pursuant to an escrow agreement, and invested in U.S. Government securities. The maturities of these securities and related earnings thereon are expected to provide sufficient cash flow to meet the debt service requirements of the defeased portion of the 1992 and 1993 Fourth Resolution Bonds as they mature. This transaction effectively released the Authority from its obligation to repay the defeased portion of the Series 1992 and 1993 Fourth Resolution Bonds and constituted an in-substance defeasance. This transaction resulted in a difference of \$50,121 between cash and securities put into escrow and the net carrying amount of the debt. This difference has been deferred and will be amortized as a component of interest expense over the remaining life of the debt. The principal outstanding is \$2,742,804 at December 31, 2001 with maturities ranging from the year 2002 to the year 2007.

4. Debt service reserve fund

During 1993, the Authority established a debt service reserve fund as required by the Series 1993A and 1993B bond resolutions to maintain a specified amount of funds to meet future debt service requirements. These requirements state that the Authority must deposit funds equal to the lesser of the maximum amount of principal and interest becoming due in any succeeding calendar year on the Series 1993A and Series 1993B Bonds or 9.9% of the initial principal amount of the Series 1993A and Series 1993B Bonds.

The 1992 and 1993 Fourth Resolution Bond Series established a debt service reserve fund as required by the Series 1992 and 1993 Fourth Resolution bond resolutions to maintain a specified amount of funds to meet future debt service requirements. These requirements state that the Authority must deposit funds equal to the lesser of the maximum amount of principal and interest becoming due in any succeeding calendar year on the Series 1992 and 1993 Fourth Resolution Bonds or 9.9% of the initial principal amount less the original issue discount on the Series 1992 and 1993 Fourth Resolution Bonds. Surety bonds issued by AMBAC Indemnity Corporation have been deposited in the Reserve Account in full satisfaction of the Reserve Account Requirements for the Series 1992 and Series 1993 Fourth Resolution Bonds.

During 1998, the Authority established a debt service reserve fund as required by the Series 1998B and 1998D bond resolutions to maintain a specified amount of funds to meet future debt service requirements. These requirements state that the Authority must deposit funds equal to the lesser of ten percent of the total principal of the loan, the maximum annual debt service or 125% of the average annual debt service for the Series 1998B and 1998D Bonds.

At December 31, 2001 the debt service reserve fund was \$5,696,514 and at December 31, 2000 the debt service reserve fund was \$5,759,357.

5. Debt service fund

The 1992 Fourth Resolution, 1993A, 1993B, 1993 Fourth Resolution, 1998B and 1998D bond resolutions require that a specified amount of funds be maintained in the debt service fund. The requirements of the debt service fund state that the Authority must deposit funds to provide for monthly interest and principal payments to start not later than six months prior to the payment of interest and twelve months prior to the payment of principal. Accordingly, the Authority had funds set aside in the debt service fund amounting to \$4,142,336 and \$4,878,389 at December 31, 2001 and 2000, respectively.

6. Future construction reserve fund

The Authority is required by the water revenue bond resolutions to maintain, on deposit, funds in the amount of one-twelfth of the subsequent year's budgeted improvement and replacement expenditures, but not less than one-twelfth of one half of 1% of the total gross cost of water plant in service and under construction. Accordingly, as the budgeted expenditures exceeded one half of 1% of water plant, the Authority was required to have reserve funds for future construction set aside in the amount of \$1,071,975 and \$840,877 at December 31, 2001 and 2000 respectively. Additionally, certain funds provided by the Series 1992, Series 1993A and 1993B Bonds are required to be maintained in this fund to pay for future acquisition and construction costs.

During 2001, and for future years, the Board has committed to pay for capital costs from available operating funds in excess of reserve requirements and other defined financial commitments.

At December 31, 2001, the future construction reserve was \$3,925,943 and at December 31, 2000 the future construction reserve was \$3,905,792.

7. Investment securities

In March 1997, the GASB issued Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* (the Statement), which establishes standards of financial accounting and reporting for certain investments held by most governmental entities and all investments held by governmental external investment pools. Included in interest income in the Statement of Net Income and Earnings Reinvested in the Business were changes in the fair value of investments of a loss of \$101,414 in 2001 and a gain of \$89,336 in 2000.

The Authority's bond resolutions allow for monies to be invested in the following instruments:

- X Obligations of the United States Government;
- X Obligations of Federal Agencies which represent full faith and credit of the United States Government;
- X Bonds issued by the Federal National Mortgage Association or the Federal Home Loan Mortgage Corporation with remaining maturities not exceeding three years;
- X Time deposits and money market accounts;
- X Commercial paper which matures not more than 270 days after the date of purchase; and
- X Municipal obligations of any state, instrumentality, or local governmental unit of such state.

The amortized cost and market value of investment securities were as follows:

	December 31, 2001		December 31, 2000	
	<u>Amortized</u>	<u>Market</u>	<u>Amortized</u>	<u>Market</u>
	<u>Cost</u>	<u>Value</u>	<u>Cost</u>	<u>Value</u>
Future construction fund				
Cash and equivalents	\$ 1,329,856	\$ 1,329,856	\$ 1,451,647	\$ 1,451,647
Mortgage-backed securities	1,049,465	1,049,919	1,817,132	1,831,220
Commercial Paper	<u>1,546,622</u>	<u>1,546,622</u>	<u>637,013</u>	<u>637,013</u>
Total	<u>\$ 3,925,943</u>	<u>\$ 3,926,397</u>	<u>\$ 3,905,792</u>	<u>\$ 3,919,880</u>
Debt service reserve fund				
Cash and equivalents	\$ 184,547	\$ 184,547	\$ 370,037	\$ 370,037
U.S. Treasury securities	1,712,676	1,712,676	1,712,676	1,712,676
Mortgage-backed securities	2,003,256	2,003,949	2,701,316	2,722,189
Commercial Paper	<u>1,796,035</u>	<u>1,796,035</u>	<u>975,328</u>	<u>975,328</u>
Total	<u>\$ 5,696,514</u>	<u>\$ 5,697,207</u>	<u>\$ 5,759,357</u>	<u>\$ 5,780,230</u>
Debt service fund				
Cash and equivalents	<u>\$ 4,142,336</u>	<u>\$ 4,142,336</u>	<u>\$ 4,878,389</u>	<u>\$ 4,878,389</u>
Total	<u>\$ 4,142,336</u>	<u>\$ 4,142,336</u>	<u>\$ 4,878,389</u>	<u>\$ 4,878,389</u>
Operating and Maintenance Fund				
Cash and equivalents	\$ 8,169,025	\$ 8,169,025	\$ 6,740,311	\$ 6,740,311
Mortgage-backed securities	6,198,223	6,200,759	8,725,344	8,795,480
Commercial Paper	<u>7,882,704</u>	<u>7,882,704</u>	<u>4,573,812</u>	<u>4,573,812</u>
Total	<u>\$ 22,249,952</u>	<u>\$ 22,252,488</u>	<u>\$ 20,039,467</u>	<u>\$ 20,109,603</u>
Total	<u>\$ 36,014,745</u>	<u>\$ 36,018,428</u>	<u>\$ 34,583,005</u>	<u>\$ 34,688,102</u>
Market Value Less Amortized Cost		<u>\$ 3,683</u>		<u>\$ 105,097</u>

8. Long-term investment

During 1990, the Authority entered into a zero coupon bond agreement which requires the Authority to make monthly deposits into an investment account through December 2008. During 1997, the Board established a policy that all earnings and proceeds to be distributed in conformance with the agreement shall be deposited into the capital fund to be used solely for future capital expenses. At December 31, 2001 and 2000, the zero coupon bond investment balance is \$8,154,128 and \$8,673,074, respectively. Interest on the investment is compounded monthly at a rate of 7.45%. The annual deposit for next year will be approximately \$456,000. The second year will be approximately \$363,000, the third year will be approximately \$277,000, the fourth year will be approximately \$197,000, and the fifth year will be approximately \$119,000. The total amount due for the two years thereafter is approximately \$70,000. On December 1, 2001 the Authority received \$1,743,267 as the second guaranteed annual payment from this investment. Varying amounts will be received each December 1 through 2008. The total amount to be received in future years is approximately \$12.1

million.

9. Pension plan and other post retirement benefits

The Authority contributes to the New York State and Local Employees Retirement System (State Plan), which is a cost-sharing, multi-employer, public employee retirement system. The State Plan provides retirement, disability, and death benefits to members as authorized by the New York State Retirement and Social Security Law. The State Plan issues publicly available financial reports that contain financial statements and required supplementary information for the State Plan. The State Plan report may be obtained by writing to the New York State and Local Retirement Systems - Employees Retirement System, Gov. Smith State Office Building, Albany, New York 12244.

Plan members who joined the State Plan before July 27, 1976 are not required to make contributions. Those joining on or after July 27, 1976 are required to contribute 3% of their annual salary for the first ten years of their membership, or credited service, in the Retirement System.

The contribution requirements of the State Plan members and the Authority are established by the New York State Retirement and Social Security Law and may be amended by the State Legislature. The Authority's contribution to the State Plan amounted to \$285,783 and \$182,174 in 2001 and 2000, respectively.

In addition to providing pension benefits, the Authority provides certain health care benefits to retired employees. The Authority's employees covered by collective bargaining units may become eligible for these benefits if they reach normal retirement age while working for the Authority for at least 15 years. For exempt employees the Authority uses a formula based on years of service and age. The Authority recognizes the cost of providing health care benefits to retired employees by expensing the annual premiums, which totaled \$472,998 and \$418,071 for 2001 and 2000, respectively.

10. Deferred compensation plan

Employees of the Authority may elect to participate in the Erie County Water Authority Deferred Compensation Plan (the Plan) created in accordance with Internal Revenue Code Section 457. The Plan permits participating employees to defer a portion of their salary until future years, usually after retirement.

Section 457 of the Internal Revenue Code was recently amended by the Small Business Job Protection Act of 1996 to require that an eligible deferred compensation plan must, by January 1, 1999, provide that all amounts deferred and the income thereon be held in trust for the exclusive benefit of participants and their beneficiaries. The Plan was amended effective October 1, 1997 to comply with the law, and the plan assets were placed into trust at that time. The plan was further amended in December 2001 to comply with the provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001, which increased contribution limits and provided new portability provisions.

11. Commitments and contingencies

The Authority maintains and operates certain facilities employed in the sale and distribution of water, which it leases from various local water district municipalities pursuant to lease management agreements. Such agreements generally are for ten-year terms, are noncancellable during the initial nine years and provide that the lessor purchase and obtain in return water exclusively from the Authority. Subsequent to its initial term, these agreements continue on a month-to-month basis until a new agreement is negotiated. Future maintenance and operating costs to be incurred by the Authority under such arrangements presently in effect are not determinable.

The Authority is subject to various laws and regulations, which primarily establishes uniform minimum national quality standards. The Authority has established procedures for the on-going evaluation of its operations to identify potential exposures and assure continued compliance with these regulatory standards.

The Authority is also committed under various operating leases for the use of certain equipment and office space. Rental expense for 2001 and 2000 aggregated \$515,236 and \$475,076, respectively. Future minimum annual rentals to be paid under such leases are not significant.

The Erie County Water Authority and the City of Tonawanda entered into a Direct Service Agreement on January 10, 2002. Included in the agreement is a commitment to invest approximately \$3,000,000 in the City of Tonawanda water system infrastructure, which will revert to the beneficial ownership of the Authority at such time that both parties have met the conditions in the executory agreement.

The Authority has committed approximately \$2,200,000 to build a pipeline and pump station within Erie County to the Genesee County line under the "Genesee County Public Supply Program." This involves a three party agreement with New York State providing a \$3,000,000 grant under its "Pipeline For Jobs" program. The Authority will receive \$1,300,000 with the balance going to Monroe County Water Authority and Genesee County for their portions of the project. The remaining balance of the Authority's commitment as of December 31, 2001 is \$2,000,000, of which \$1,100,000 will be funded by the remaining portion of the state grant.

The Authority is involved in litigation and other matters arising in its normal operating, financing, and investing activities. While the resolution of such litigation or other matters could have a material effect on earnings and cash flows in the year of resolution, none of this litigation, and none of these other matters, are expected to have a material effect on the financial condition of the Authority at this time.



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