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Independent Auditors' Report

Members of the Board
The Harrisburg Authority:

We have audited the financial statements of The Harrisburg Authority (a component unit of the City of Harrisburg, Pennsylvania) as of and for the year ended December 31, 1999, as listed in the accompanying table of contents. These financial statements are the responsibility of The Harrisburg Authority's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Harrisburg Authority at December 31, 1999, and the results of its operations and cash flows for the year then ended in conformity with generally accepted accounting principles.

The waste incinerator, operated by the Resource Recovery Facility of The Harrisburg Authority, is required by the Environmental Protection Agency to undertake a modernization program prior to December 1, 2000, to maintain operations in its present capacity. It is probable that this modernization will not occur prior to December 1, 2000, and alternative methods of operation, which are currently under consideration, will be necessary at that time. Additionally, the Resource Recovery Fund has experienced significant operating losses and has an accumulated deficit of \$13,494,792 at December 31, 1999. These issues are discussed further in note 11 to the financial statements.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The combining financial statements listed in the accompanying table of contents are presented for purposes of additional analysis rather than to present the financial position and results of operations of the individual funds. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

KPMG LLP

May 25, 2000



KPMG LLP KPMG LLP, a US limited
a member of KPMG International, a

THE HARRISBURG AUTHORITY
(a component unit of the City of Harrisburg, Pennsylvania)

Notes to Financial Statements

December 31, 1999

(10) Inter-fund Transfers

During 1999, pursuant to settlement of certain litigation with the Environmental Protection Agency and Bethlehem Steel, certain amounts, which had been received and held in the Administrative Fund, were transferred to the Sewer Fund. The Sewer Fund then reimbursed the Administrative Fund for certain expenses related to this litigation, and subsequently all inter-fund payables were considered satisfied. In addition, \$578,238 received as current year settlements of the litigation was deposited in the Sewer Fund and recorded as an increase in construction obligations.

(11) Commitments and Contingencies

(a) Resource Recovery Fund

The Authority is required to undertake a modernization program of its waste incinerator operated by the Resource Recovery Facility before December 1, 2000 to enable the incinerator to meet standards required by the Environmental Protection Agency. The cost of this modernization program is estimated to be approximately \$150,000,000. It is probable that waste processing contracts and related funding for these improvements will not be available prior to December 1, 2000.

Authority and City of Harrisburg management are continuing to pursue a number of alternatives which would support the continued operations of the Resource Recovery Facility. These include the possible reduction in the capacity of waste incinerated, which would allow for continued operation of the incinerator at the reduced capacity for another five years. In addition, a transfer station has been constructed as an operational backup for excess, or all capacity.

If the facility fails to generate sufficient revenues to pay debt service on the ~~Resource Recovery Facility Bonds, Series A, 1993, and Series B, 1998~~, or ceases revenue generating operations, the City of Harrisburg will be required to pay principal of and interest on such bonds when due pursuant to a Guaranty Agreement among the City, the Authority, and the trustee for the bonds. The Resource Recovery Fund has incurred substantial accumulated losses, which have caused the Fund to experience cash flow difficulties.

When the Authority purchased the Resource Recovery Facility from the City in 1993, the Authority paid the City approximately \$30 million in consideration. The Agreement of Sale allows for a maximum purchase price of \$55 million, with the final purchase price to be based on the financial capability of the Resource Recovery Facility. The balance of the purchase price is to be paid to the City out of proceeds of the subsequent additional financing which will also fund the improvements necessary to modernize the facility as discussed above, if sufficient contracts are entered into by the Authority to justify the additional debt.

(b) Other

As of December 31, 1999, the Authority has commitments of approximately \$4,400,000 under contracts for improvements to the water-metering systems.

The Authority is involved in several lawsuits arising in the normal course of business. It is the opinion of management that any liabilities resulting from these proceedings would not materially affect the financial position of the Authority at December 31, 1999.