KPMG

MASSACHUSETTS WATER RESOURCES AUTHORITY

Financial Statements and Supplemental Schedules
and Required Supplementary Information

June 30, 2014 and 2013

(With Independent Auditors' Report Thereon)

MASSACHUSETTS WATER RESOURCES AUTHORITY

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KPMG LLP
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Boston, MA 02111

Independent Auditors' Report

The Board of Directors
Massachusetts Water Resources Authority:

Report on the Financial Statements

We have audited the accompanying statements of net position of the Massachusetts Water Resources Authority (the Authority), as of June 30, 2014 and 2013, and the statements of revenues, expenses, and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority at June 30, 2014 and 2013, and the changes in net position and cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 10 and schedules of funding progress on page 45 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary and Other Information

Our audit was conducted for the purpose of forming an opinion on the Authority's basic financial statements. The supplemental schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The supplemental schedules listed in the table of contents are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplemental schedules listed in the table of contents are fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated August 25, 2014 on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.

KPMG LLP

Boston, Massachusetts
August 25, 2014

This section of the Authority's annual financial report presents our discussion and analysis of the Authority's financial performance during the Fiscal Years ended June 30, 2014 and 2013. Please read it in conjunction with the Authority's financial statements, which immediately follow this section.

Financial Highlights – Fiscal Year 2014

The Fiscal Year 2014 customer service revenues were approximately $639.7 million. Of this amount, rate revenues represent approximately 98.3%, or $628.7 million, and were $21.2 million higher than Fiscal Year 2013. This was due to an increase in assessments.

Total operating expenses, excluding depreciation, were approximately $273.5 million in Fiscal Year 2014. The 2.3% increase in total operating expenses over Fiscal Year 2013 is the result of increases in personnel costs, maintenance and pension costs. Pension expense increased as an additional, optional $5 million contribution was made in Fiscal Year 2014, as well as a $1.6 million payment that reflects recognition of the projected increases associated with revised mortality tables.

Net nonoperating expenses decreased $14.3 million, or 6.0%, due to an $8.5 million increase in investment income, a $5 million decrease in interest expense and receipt of $.8 million of debt service assistance. The increase in investment income was due to a changing portfolio of investments, yielding a smaller unrealized loss on investments.

Total assets at June 30, 2014 were approximately $8.1 billion, a $155.3 million, or 1.9%, decrease over total assets at June 30, 2013.

During Fiscal Year 2014, the Authority issued direct-purchase General Revenue Refunding Bonds, 2014 Series A and 2014 Series B for a total of $114.8 million. The proceeds from these bonds were used to refund $114.8 million of the Authority's outstanding bonds. The interest rate on these bonds was 0.44% to 0.59% during Fiscal Year 2014.

Total capital assets (net of depreciation) were approximately $6.1 billion at June 30, 2014, a $80.8 million, or 1.3%, decrease over June 30, 2013. The decrease was primarily due to the rate of depreciation being higher than the rate of capitalization.

Financial Highlights – Fiscal Year 2013

The Fiscal Year 2013 customer service revenues were approximately $617.4 million. Of this amount, rate revenues represent approximately 98.4%, or $607.5 million, and were $17.8 million higher than Fiscal Year 2012. This was due to an increase in assessments.

Total operating expenses, excluding depreciation, were approximately $267.4 million in Fiscal Year 2013. The 2.2% increase in total operating expenses over Fiscal Year 2012 is the result of increases in personnel costs, other materials and pension costs. Other material costs increased due to the purchase of new mobile and handheld radios to complete the conversion to digital transmission. Pension expense increased as an additional, optional $4.7 million contribution was made in Fiscal Year 2013.

(Continued)

Net nonoperating expenses decreased $19.9 million, or 7.7%, due to a $24 million decrease in investment income and a $44.3 million decrease in interest expense. A $400,000 debt service grant in Fiscal Year 2012 comprises the remaining difference. The decrease in investment income was due to an increase in the unrealized loss on fixed rate investments due to higher market rates at June 30. The decrease in interest expense was due to reclassification in Fiscal Year 2012 for regulatory accounting provisions.

Total assets at June 30, 2013 were approximately $8.3 billion, a $145.8 million, or 1.7%, decrease over total assets at June 30, 2012.

During Fiscal Year 2013, the Authority issued direct-purchase General Revenue Refunding Bonds, 2012 Series E, 2012 Series F and 2012 Series G for a total of $180.9 million. The proceeds from these bonds were used to refund $180.9 million of the Authority's outstanding bonds. The interest rate on these bonds was 0.61% to 0.93% during Fiscal Year 2013. The Authority also issued General Revenue Refunding Bonds, 2013 Series A for $170.6 million. The proceeds from these bonds were used to refund $175.6 million of the Authority's outstanding bonds. The interest rate on these bonds is 3% to 5%.

Total capital assets (net of depreciation) were approximately $6.2 billion at June 30, 2013, a $78.5 million, or 1.3%, decrease over June 30, 2012. The decrease was primarily due to the capitalization of community-owned CSO projects from construction in progress to other assets.

In Fiscal Year 2013 the Authority implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources*, and *Net Position* and GASB Statement No. 65, Items Previously Reported as Assets and Liabilities. These financial statements now contain Statements of Net Position. Deferred outflows from hedging derivative instruments and deferred losses on bond refundings are now reported as deferred outflows of resources. Deferred losses on bond refundings were previously reported as a reduction to long-term debt. Additionally, amounts previously reported as deferred credits in accordance with regulatory accounting provisions are now reported as deferred inflows from regulated activities.

Overview of the Financial Statements

The financial section of this annual report consists of three parts: management's discussion and analysis (this section), the financial statements and related notes to the financial statements, required supplementary information, and other supplementary information.

The financial statements provide both long-term and short-term information about the Authority's overall financial status. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of other supplementary information that further explains and supports the information in the financial statements.

Financial Analysis of the Authority

Net Position

The Authority's total net position at June 30, 2014 was approximately $1.8 billion, a $38.8 million decrease from June 30, 2013. Total assets decreased $155.3 million, or 1.9%, to $8.1 billion, and total liabilities decreased $115.7 million, or 1.8%, to $6.5 billion.

The Authority's total net position at June 30, 2013 was approximately $1.8 billion, a $38.1 million decrease from June 30, 2012. Total assets decreased $145.8 million, or 1.7%, to $8.3 billion, and total liabilities decreased $129.3 million, or 1.9%, to $6.6 billion.

Net Position
(Dollars in thousands)

		2014	2013	2012*	Percentage change 2014–2013	Percentage change 2013–2012
Current assets	$	126,567	125,159	117,332	1.1%	6.7%
Restricted assets		718,750	762,951	869,715	(5.8)	(12.3)
Capital assets		6,073,139	6,153,926	6,232,394	(1.3)	(1.3)
Other assets		1,197,311	1,229,006	1,197,421	(2.6)	2.6
Total assets		8,115,767	8,271,042	8,416,862	(1.9)	(1.7)
Deferred outflows of resources from derivative instruments		40,977	43,867	92,381	(6.6)	(52.5)
Deferred outflows of resources from refunded debt		73,617	87,360	84,132	(15.7)	3.8
Current liabilities		371,594	328,837	300,868	13.0	9.3
Payable from restricted assets		217,707	204,905	202,306	6.2	1.3
Long-term debt		5,697,812	5,876,695	5,998,205	(3.0)	(2.0)
Long-term lease		30,938	31,700	32,404	(2.4)	(2.2)
Other liabilities		148,803	140,422	178,119	6.0	(21.2)
Total liabilities		6,466,854	6,582,559	6,711,902	(1.8)	(1.9)
Deferred inflows of resources		7,092	24,543	48,226	(71.1)	(49.1)
Net position:						
Net investment in capital assets		774,390	755,266	845,989	2.5	(10.7)
Restricted		271,424	307,208	293,373	(11.6)	4.7
Unrestricted		710,601	732,693	693,885	(3.0)	5.6
Total net position	$	1,756,415	1,795,167	1,833,247	(2.2)%	(2.1)%

* Certain amounts were reclassified to conform to the fiscal 2013 presentation.

Changes in Net Position

The decrease in net position at June 30, 2014 was $38.8 million, or 2.2%, as compared with June 30, 2013. The Authority's total operating revenues increased by 3.9% to $648 million and total operating expenses increased 2.3% to $273.5 million.

The decrease in net position at June 30, 2013 was $38.1 million, or 2.1%, as compared with June 30, 2012. The Authority's total operating revenues increased by 3.4% to $623.4 million and total operating expenses increased 2.2% to $267.4 million.

Changes in Net Position
(Dollars in thousands)

	2014	2013	2012*	Percentage change 2014–2013	Percentage change 2013–2012
Operating revenues:					
Customer service revenues	$ 639,691	617,415	599,372	3.6%	3.0%
Other revenues	8,326	5,978	3,248	39.3	84.1
Total operating revenues	648,017	623,393	602,620	3.9	3.4
Operating expenses:					
Operations	100,778	101,425	99,802	(0.6)	1.6
Maintenance	29,453	26,956	26,776	9.3	0.7
Payments in lieu of taxes	7,872	7,640	7,311	3.0	4.5
Engineering, general, and administrative	135,401	131,329	127,621	3.1	2.9
Total operating expenses	273,504	267,350	261,510	2.3	2.2
Depreciation and amortization	193,062	190,852	191,124	1.2	(0.1)
Operating income	181,451	165,191	149,986	9.8	10.1
Nonoperating items:					
Regulatory accounting provisions	(3,808)	23,917	57,229	(115.9)	(58.2)
Net nonoperating expenses	(225,293)	(239,616)	(259,537)	(6.0)	(7.7)
Capital grants and contributions	5,958	6,630	7,696	(10.1)	(13.9)
Changes in derivative related accounts	2,940	5,798	2,940	(49.3)	97.2
Total nonoperating items	(220,203)	(203,271)	(191,672)	8.3	6.1
Change in net position	(38,752)	(38,080)	(41,686)	1.8	(8.7)
Total net position – beginning of year	1,795,167	1,833,247	1,874,933	(2.1)	(2.2)
Total net position – end of year	$ 1,756,415	1,795,167	1,833,247	(2.2)%	(2.1)%

* Certain amounts were reclassified to conform to the fiscal 2013 presentation.

During Fiscal Year 2014, the increases in customer service revenues were primarily due to the 3.49% increase in the rate revenue requirement ($21.2 million).

During Fiscal Year 2013, the increases in customer service revenues were primarily due to the 3.0% increase in the rate revenue requirement ($17.8 million).

Total operating costs, before depreciation and amortization, were approximately $273.5 million in Fiscal Year 2014. The 2.3% increase in total operating expenses over Fiscal Year 2013 is the result of increases in personnel costs, maintenance and pension costs. Pension expense increased as an additional, optional $5 million contribution, as well as a $1.6 million payment that reflects recognition of the projected increases associated with revised mortality tables were made in Fiscal Year 2014

Total operating costs, before depreciation and amortization, were approximately $267.4 million in Fiscal Year 2013. The 2.2% increase in total operating expenses over Fiscal Year 2012 is the result of increases in personnel costs, other materials and pension costs. Pension expense increased as an additional, optional $4.7 million contribution was made in Fiscal Year 2013.

In Fiscal Year 2014, net nonoperating expenses decreased $14.3 million, or 6.0%, due to a $8.5 million increase in investment income, a $5 million decrease in interest expense and receipt of $0.8 million of debt service assistance. The increase in investment income was due to a changing portfolio of investments, yielding a smaller unrealized loss on investments.

In Fiscal Year 2013, net nonoperating expenses decreased $19.9 million, or 7.7%, due to a $24 million decrease in investment income and a $44.3 million decrease in interest expense. A $400,000 debt service grant in Fiscal Year 2012 comprises the remaining difference. The decrease in investment income was due to an increase in the unrealized loss on fixed rate investments due to higher market rates at June 30. The decrease in interest expense was due to reclassifications in Fiscal Year 2012 for regulatory accounting provisions.

Operating Costs by Functionality
(Dollars in thousands)

		2014	2013	2012	Percentage change 2014–2013	Percentage change 2013–2012
Wastewater treatment and transport	$	94,703	96,255	95,137	(1.6)%	1.2%
Water treatment and transport		35,395	34,702	33,762	2.0	2.8
Water and wastewater quality		7,731	7,430	7,815	4.1	(4.9)
Metering and monitoring		6,094	5,845	5,511	4.3	6.1
Facilities planning, design, and construction		9,318	9,337	9,604	(0.2)	(2.8)
Management information systems		10,325	9,115	8,901	13.3	2.4
Administration and support		47,997	45,923	44,105	4.5	4.1
Total direct operating costs		211,563	208,607	204,835	1.4	1.8
Indirect operating costs		61,941	58,743	56,675	5.4	3.6
Total operating costs	$	273,504	267,350	261,510	2.3%	2.2%

Wastewater treatment and transport expenses decreased due to a higher level of non-capitalizable equipment purchases in the prior year. Water treatment and transport expenses increased due to increases in salaries and wages and electricity. Water and wastewater quality expenses increased due to increased Harbor Outfall Monitoring activities. Metering and monitoring expenses increased due to purchases of equipment. Management information systems costs increased to due additional purchases of computer hardware, software and related maintenance services. Administration and support expenses increased due to higher health insurance and workers' compensation expenses, as well as increased non-capitalizable inventory purchases.

Capital Assets and Debt Administration

Capital Assets

As of June 30, 2014 and 2013, the Authority had $6.1 billion and $6.2 billion of capital assets (net of depreciation), respectively. This includes land, construction in progress, plant and equipment for the water and sewer systems, furniture and fixtures, leasehold improvements, and motor vehicles and equipment. The Authority's net capital assets decreased approximately $80.8 million, or 1.3%, during Fiscal Year 2014, primarily due to the rate of depreciation being higher than the rate of capitalization.

Capital Assets
(Net of depreciation, dollars in thousands)

	2014	2013	2012	Percentage change 2014–2013	Percentage change 2013–2012
Land	$ 23,741	23,733	24,255	—%	(2.2)%
Construction in progress	193,180	163,916	159,878	17.9	2.5
Plant and equipment, water, and sewer systems	5,852,085	5,962,858	6,045,143	(1.9)	(1.4)
Furniture and fixtures	425	750	1,033	(43.3)	(27.4)
Leasehold improvements	327	339	351	(3.5)	(3.4)
Motor vehicles and equipment	3,381	2,330	1,734	45.1	34.4
	$ 6,073,139	6,153,926	6,232,394	(1.3)%	(1.3)%

Debt Administration

The Authority's bond sales must be approved by its board of directors (the Board) and must comply with rules and regulations of the United States Treasury Department. Neither the Commonwealth of Massachusetts (the Commonwealth) nor any political subdivision thereof shall be obligated to pay the principal of, or premium or interest on, any debt outstanding and neither the faith and credit nor the taxing power of the Commonwealth or any political subdivision thereof is pledged to such payment.

Bond Resolutions

Pursuant to its general bond resolution, the Authority must comply with a rate covenant that requires it to set rates to maintain revenues sufficient to pay: current expenses; debt service on indebtedness; required deposits to reserves; costs of maintenance, replacement, and/or improvements to the wastewater and water systems that are considered current expenses and any additional amounts the Authority may be required to pay by any law or contract.

In addition to the rate covenant, the Authority is required to meet two covenants with respect to debt service coverage. The primary debt service coverage requires that the Authority fix and adjust rates and charges to provide revenues available for bond debt service in an amount equal to 1.2 times that is required for debt service on all outstanding bonds, not including subordinated bonds. The subordinated debt service coverage requires that the Authority fix and adjust rates and charges to provide revenues available for bond debt service in an amount equal to 1.1 times that is required for debt service on all outstanding bonds, including subordinated bonds.

Credit Rating

The Authority's $3.5 billion Senior Lien General Revenue Bonds are rated Aa1 from Moody's Investors Service, AA+ by Standard and Poors Ratings Services and AA+ from FitchRatings. The $1.0 billion Subordinate Lien General Revenue Bonds are rated Aa2 from Moody's Investors Service, AA by Standard and Poors Ratings Services and AA from FitchRatings. Some of the Authority's revenue bonds are enhanced by bond insurance. The credit ratings of these bond series will be the higher rating of either the Authority or the firm providing the enhancement. In the case of bonds enhanced by a letter of credit, the rating will be the highest of the Authority's, the provider or, if available, a joint rating. The subordinated debt of $1.0 billion with the Massachusetts Water Pollution Abatement Trust is not rated as the Authority's debt.

Economic Factors and Next Year's Budget

In June 2014, the Board approved the Fiscal Year 2015 Current Expense Budget (CEB), which totals $674.5 million in expenses.

The $674.5 million expense total is comprised of $409.8 million (60.8%) in capital financing costs and $264.7 million (39.2%) in operating expenses, of which $217.2 million (82%) is for direct expenses and $47.5 million (18%) is for indirect expenses. The total represents an increase of $20.1 million from Fiscal Year 2014 spending, which is comprised of $6.7 million in higher operating costs and $13.4 million in higher debt service costs.

The Fiscal Year 2015 rate revenue requirement approved by the Board is $650.3 million; an increase of 3.43% compared with the Fiscal Year 2014 budget.

Fiscal Year 2015 budgeted nonrate revenue totals $24.2 million, a decrease of $10.8 million from actual Fiscal Year 2014 nonrate revenue. The nonrate revenue budget is comprised of $9.7 million in investment income, $13.8 million in other user charges and other revenue and $.7 million in entrance fees.

CIP 10 Year Plan

The Authority's planned spending for capital improvements in future years reflects the Authority's ongoing efforts to upgrade and maintain the system and to align its project prioritization process with the Master Plan.

Major planned and ongoing projects include:

- Improvement and replacement of equipment on Deer Island and at major headworks facilities to ensure continued efficient and effective operations.
- Completion of the long-term CSO control plan, resulting in closing CSO outfalls and reducing CSO discharges to Boston Harbor and the Mystic, Charles, and Neponset River systems.
- Commitment to long-term redundancy plan for the metropolitan water tunnel system and an emergency pump station at the Wachusett reservoir.
- Completion of covered storage facilities to provide safe, reliable storage for water treated at John J. Carroll water treatment plan and transported through the MetroWest Tunnel and Hultman Aqueduct.
- Dedication to using resources efficiently, responding to climate change and reducing the environmental impacts of the Authority's daily operations by installing alternative energy sources and promotion of improved self-generation.
- Enhanced commitment to the community assistance programs for both the sewer and water systems to improve local infrastructure by adding two new phases of the Infiltration and Inflow program totaling $160 million.
- Continued investment for the upgrade of Management Information Systems to ensure the availability, integrity and security of data.
- Commence the Residuals Asset Protection program for maintaining and improving the operations and infrastructure of the biosolids processing in the long term.
- Commencement of a pilot program to determine potential benefit and costs of co-digestion of pre-processed organics in the Deer Island digesters.

Contacting the Authority's Financial Management

This report is designed to provide our bondholders, member communities and other interested parties with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the revenue it receives. If you have questions about this report or need additional information, contact the Massachusetts Water Resources Authority, Administration and Finance Division, 100 First Avenue, Boston, MA 02129.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Statements of Net Position

June 30, 2014 and 2013

(Dollars in thousands)

Assets	**2014**	**2013**
Unrestricted current assets:		
Cash and cash equivalents (note 4)	$ 57,488	45,961
Investments (note 4)	37,769	48,819
Intergovernmental loans (note 7)	30,304	29,768
Accounts receivable	1,006	611
Total unrestricted current assets	126,567	125,159
Restricted assets:		
Investments (note 4)	716,208	759,498
Interest receivable	2,542	3,453
Total restricted assets	718,750	762,951
Capital assets:		
Capital assets – not being depreciated (note 8)	216,921	187,649
Capital assets – being depreciated – net (note 8)	5,856,218	5,966,277
Total capital assets	6,073,139	6,153,926
Regulatory assets (note 3)	797,591	818,680
Other assets, net (note 7)	399,720	410,326
Total assets	8,115,767	8,271,042
Deferred Outflows of Resources		
Deferred outflows from derivative instruments (note 6)	40,977	43,867
Deferred outflows from refunding debt	73,617	87,360
Liabilities		
Current liabilities:		
Accounts payable and accrued expenses	59,434	54,849
Commercial paper notes (note 6)	170,000	144,000
Current portion of long-term debt (note 6)	142,160	129,988
Total current liabilities	371,594	328,837
Payable from restricted assets:		
Accounts payable for construction	28,635	17,023
Accrued interest on bonds payable	86,983	85,963
Reserves (note 5)	102,089	101,919
Total payable from restricted assets	217,707	204,905
Retainage on construction in progress	5,823	8,073
Long-term debt – less current portion (note 6)	5,697,812	5,876,695
Long-term capital lease (note 9)	30,938	31,700
Other postemployment benefits (note 11)	102,003	88,482
Liability for derivative instruments (note 6)	40,977	43,867
Total liabilities	6,466,854	6,582,559
Deferred Inflows of Resources		
Deferred inflows from regulated activities (note 3)	7,092	24,543
Net Position		
Net investment in capital assets	774,390	755,266
Restricted	271,424	307,208
Unrestricted	710,601	732,693
Total net position	$ 1,756,415	1,795,167

Commitments and contingencies (notes 9, 10, 11, 12, and 13)

See accompanying notes to financial statements.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Statements of Revenues, Expenses, and Changes in Net Position

Years ended June 30, 2014 and 2013

(Dollars in thousands)

		2014	2013
Operating revenues (note 2):			
Customer services	$	639,691	617,415
Other		8,326	5,978
Total operating revenues		648,017	623,393
Operating expenses:			
Operations		100,778	101,425
Maintenance		29,453	26,956
Payments in lieu of taxes		7,872	7,640
Engineering, general, and administrative		135,401	131,329
Total operating expenses		273,504	267,350
Income from operations before depreciation		374,513	356,043
Depreciation and amortization		193,062	190,852
Operating income		181,451	165,191
Regulatory accounting provisions:			
Change in reserves (note 5)		(170)	(1,398)
Change in regulatory provisions, net (note 3)		(3,638)	25,315
Total regulatory accounting provisions		(3,808)	23,917
Nonoperating revenues (expenses):			
Debt service grant		854	—
Investment income (loss)		5,433	(3,079)
Interest expense		(231,580)	(236,537)
Changes in derivative related accounts		2,940	5,798
Total nonoperating expenses		(222,353)	(233,818)
Net loss before capital contributions		(44,710)	(44,710)
Capital grants and contributions		5,958	6,630
Decrease in net position		(38,752)	(38,080)
Total net position, beginning of year		1,795,167	1,833,247
Total net position, end of year	$	1,756,415	1,795,167

See accompanying notes to financial statements.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Statements of Cash Flows

Years ended June 30, 2014 and 2013

(Dollars in thousands)

		2014	2013
Cash flows from operating activities:			
Cash received from customers	$	639,306	617,807
Cash paid to suppliers for goods and services		(119,056)	(119,266)
Cash paid to employees for services		(128,816)	(122,179)
Cash paid in lieu of taxes		(7,872)	(7,640)
Other operating receipts		8,286	6,065
Net cash provided by operating activities		391,848	374,787
Cash flows from capital and related financing activities:			
Proceeds from sale of revenue bonds, loans, and notes		151,146	111,852
Capital grants for construction		5,958	6,630
Debt service grant		854	—
Capital lease principal payments		(762)	(705)
Capital lease interest payments		(2,455)	(2,512)
Repayment of debt		(274,415)	(199,130)
Interest paid on debt		(228,522)	(232,954)
Plant expenditures		(92,808)	(156,937)
Net cash used for capital and related financing activities		(441,004)	(473,756)
Cash flows from investing activities:			
Purchases of short-term investments		(3,936)	(206,118)
Sales and maturities of short-term investments		72,050	135,000
Changes in restricted money market investments		(20,011)	161,152
Interest received		12,580	12,659
Net cash provided by investing activities		60,683	102,693
Net increase in cash and cash equivalents		11,527	3,724
Cash and cash equivalents, beginning of year		45,961	42,237
Cash and cash equivalents, end of year	$	57,488	45,961
Reconciliation of operating income to net cash provided by operating activities:			
Operating income	$	181,451	165,191
Adjustments to reconcile operating income to net cash provided by operating activities:			
Depreciation and amortization		193,062	190,852
Change in other accounts		(431)	133
Change in accounts payable		17,766	18,611
Net cash provided by operating activities	$	391,848	374,787

Noncash capital and related financing activities:

In fiscal 2014, general revenue refunding bonds in the aggregate principal amount of $114,755 were issued to defease $114,755 of bonds outstanding.

In fiscal 2013, general revenue refunding bonds in the aggregate principal amount of $284,840 were issued to defease $289,800 of bonds outstanding.

See accompanying notes to financial statements.

(1) Organization

The Massachusetts Water Resources Authority (the Authority) was established in January 1985 pursuant to Chapter 372 (the Enabling Act) of the Act of 1984 of the Commonwealth of Massachusetts (the Commonwealth). The Authority, a successor agency to certain functions of the Metropolitan District Commission (the MDC) (which became part of the Department of Conservation and Recreation (the DCR) in July 2003), is a public instrumentality and, effective July 1, 1985, provides water supply services and sewage collection, treatment, and disposal services to areas of the Commonwealth.

The Authority is governed by an 11-member board of directors (the Board) chaired by the Secretary of Energy and Environmental Affairs for the Commonwealth. The Secretary and two other members are appointed by the Governor. Three members of the Board are appointed by the Mayor of Boston and three are appointed by the Authority’s Advisory Board. One member is appointed by the Mayor of Quincy and one by the Winthrop Council President.

(2) Summary of Significant Accounting Policies

The accounting policies of the Authority conform to U.S. generally accepted accounting principles as applicable to government enterprises. The following is a summary of the Authority’s significant accounting policies:

(a) Basis of Presentation

The Authority is required by the Enabling Act to establish user rates for its water and sewer services which provide sufficient funds to recover the costs of operations (excluding depreciation), debt service, maintenance, replacements, improvements to its facilities, and appropriate reserves. The Authority’s financial statements are reported on the accrual basis of accounting and the economic measurement focus as specified by the Governmental Accounting Standards Board’s (GASB) requirements for an enterprise fund.

The Authority distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing water and sewer services to its member communities. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. All operating revenues are pledged for repayment of outstanding debt service.

In addition, the Authority applies the provisions of GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, to provide a better matching of revenues and expenses. The effect of this policy has been to defer certain outflows of resources, which will be recovered through future revenues in accordance with the Authority’s rate model, and to record deferred inflows of resources for revenue collected through current rates for costs expected to be incurred in the future. The effects of the Authority’s accounting policies are discussed further in note 3.

(b) Capital Assets

On July 1, 1985, ownership of the MDC's sewer and waterworks personal property was transferred to the Authority. Pursuant to the Enabling Act, ownership of the real property of the MDC sewer and waterworks systems was not transferred from the Commonwealth to the Authority; however, the Authority has the right to use, improve, maintain, and manage that property. In addition, ownership of the real and personal property of the watershed system remains with the Commonwealth; however, the Authority has the right to utilize the water therefrom for water supply purposes.

The personal property, together with the rights to the real property and watershed system, was recorded at its estimated fair value of $2,331,465 (including certain construction projects which were in progress as of July 1, 1985), based upon an appraisal performed by valuation specialists. Property, plant, and equipment acquired or constructed since July 1, 1985, is stated at historical cost, and includes the expenditure of capital grants in aid of construction.

Betterments and major renewals are capitalized and included in capital asset accounts, while expenditures for maintenance and repairs are charged to expense when incurred. The cost of depreciable assets and related accumulated depreciation is eliminated from the accounts when such items are disposed of or otherwise retired.

(c) Interest Cost and Principal Payments on Construction

During Fiscal Years 2014 and 2013, none of the Authority's interest expense was capitalized to construction in progress in accordance with its current policy of recovering such costs through rates as incurred. Rates collected for principal payments on debt related to assets under construction are deferred until the related asset is completed and depreciation commences.

(d) Depreciation

The Authority provides for depreciation by use of the straight-line method. Depreciation is intended to distribute the cost of depreciable properties, including those financed by capital grants in aid of construction, over the following estimated average useful lives:

	Years
Plant and equipment, water and sewerage systems	5–100
Motor vehicles and equipment	5
Furniture and fixtures	7
Leasehold improvements	3–5

(e) Revenue Recognition

The Authority recognizes revenue as amounts become collectible from its customers for water and sewer services provided. The majority of the Authority's billings to cities and towns are subject to, in the event of nonpayment, the local aid intercept allowed by the Enabling Act.

(Continued)

(f) Cash and Cash Equivalents

The Authority's policy is to treat unrestricted investments with a maturity date of three months or less when purchased as cash equivalents for purposes of the statements of cash flows. Restricted cash and cash equivalents are combined with investments on the statements of net position, and shown separately on the statements of cash flows as an investing activity.

(g) Payments in Lieu of Taxes

The Enabling Act authorizes and directs the Authority to pay to the DCR (formerly the MDC) Division of Watershed Management, who in turn remits payment to each city or town in which land of the Quabbin watershed and Ware River watershed is located. Each such payment is equal to the amount which the respective city or town would receive in property taxes, based upon the fair value of such land if such land were not tax exempt.

(h) Investments

Investments, other than guaranteed investment contracts, are recorded at fair value. Fair value is determined based on quoted market price. Guaranteed investment contracts are recorded at cost. The Authority recorded unrealized losses of $6,699 in Fiscal Year 2014 and $16,672 in Fiscal Year 2013 as part of investment income.

(i) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

(j) Compensated Absences

Employees of the Authority may accumulate unused sick time of which 30% will be paid in cash upon retirement from the Authority. The liability for vacation leave is based on the amount earned but not used; for sick leave, it is based on a percentage of the amount accumulated at the statement of net position dates. The liability for both amounts is calculated based on the pay or salary rates in effect at the statements of net position dates.

(3) Regulatory Assets and Deferred Inflows from Regulatory Activities

In accordance with GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, regulatory assets and deferred inflows from regulatory activities result primarily from differences between depreciation on property, plant, and equipment not financed by grants or capital contributions, which is recovered through rates as principal payments on debt service, and from amounts determined by the Board to be utilized in a subsequent year to reduce customer billings (rate stabilization).

(Dollars in thousands)

A summary of the activity of regulatory assets and deferred inflows for Fiscal Years 2014 and 2013 is as follows:

		Sewer	Water	Total
Balance – June 30, 2012 – net	$	639,910	128,912	768,822
Difference between depreciation of capital assets not financed by grants or capital contributions, and debt service in excess of interest expense		(866)	2,499	1,633
Other – net		15,322	8,360	23,682
Balance – June 30, 2013 – net		654,366	139,771	794,137
Difference between depreciation of capital assets not financed by grants or capital contributions, and debt service in excess of interest expense		(21,060)	(29)	(21,089)
Other – net		15,922	1,529	17,451
Balance – June 30, 2014 – net	$	649,228	141,271	790,499

The net balance at June 30, 2014 and 2013 is presented on the statements of net position as follows:

		2014	2013	Current year change
Regulatory assets	$	797,591	818,680	(21,089)
Deferred inflows from regulatory activities		(7,092)	(24,543)	17,451
Net change	$	790,499	794,137	(3,638)

The balance in the rate stabilization reserve was $36,512 at June 30, 2014 and $40,012 at 2013.

(4) Deposits and Investments

The following represents essential risk information about the Authority’s deposits and investments:

(a) Custodial Credit Risk – Deposits

The custodial credit risk for deposits and certificates of deposit is the risk that, in the event of a bank failure, the Authority’s deposits may not be recovered. The deposits in the bank in excess of the insured amount are uninsured and uncollateralized.

The bank deposits at June 30, 2014 and 2013 were $58,008 and $47,191, respectively. Of these amounts, $57,758 and $46,941 were exposed to custodial credit risks as uninsured and uncollateralized.

(Dollars in thousands)

(b) Investments

The Authority is authorized by its general bond resolution to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, bonds, or notes of public agencies or municipalities, bank time deposits, guaranteed interest contracts, money market accounts, interest rate swap agreements, and repurchase agreements. All investments are held by a third-party in the Authority's name. These investments are recorded at fair value.

The following guaranteed investment contract was in force as of June 30, 2014 and 2013, respectively. Such contracts are fully collateralized and recorded at cost:

Investment agreement provider	Rate	Maturity	2014	2013
Wells Fargo Bank, N.A.	5.17%	August 1, 2016	$ 14,456	14,456
Total			$ 14,456	14,456

(c) Credit Ratings

All debt securities purchased, such as FNMA, FHLMC, and FHLB issues have historically had a credit rating of AAA or they have been collateralized to AAA. On August 8, 2011, Standard & Poor's reduced the credit rating for these agencies to AA+. The reduction in credit rating did not affect the Authority's bond covenants or escrow requirements.

The guaranteed investment contracts and money market funds are not rated.

The general bond resolution limits the Authority to investing in securities that are rated in the three highest rating categories as defined by S&P and Moody's.

(d) Concentration Risk

The Authority has no investments, at fair value, which exceeds 5% of the Authority's total investments as of June 30, 2014 and 2013.

(Dollars in thousands)

(e) Interest Rate Risk

The following is a listing of the Authority's fixed income investments and related maturity schedule as of June 30, 2014 and 2013:

June 30, 2014

		Investment maturities (in years)			
Investment type	**Fair value**	**<1**	**1–3**	**4–8**	**>9**
Money market mutual funds	$ 479,170	479,170	—	—	—
U.S. agency obligations	260,351	—	—	43,497	216,854
Guaranteed investment contract	14,456	—	14,456	—	—
Total	$ 753,977	479,170	14,456	43,497	216,854

June 30, 2013

		Investment maturities (in years)			
Investment type	**Fair value**	**<1**	**1–3**	**4–8**	**>9**
Money market mutual funds	$ 459,159	459,159	—	—	—
U.S. Treasury notes and bonds	4,096	4,096	—	—	—
U.S. agency obligations	330,606	70,006	—	39,433	221,167
Guaranteed investment contract	14,456	—	—	14,456	—
Total	$ 808,317	533,261	—	53,889	221,167

The Authority's bond resolution limits maturities to less than 15 years. The majority of the Authority's investments are held in short-term money market funds and long-term investments in U.S. agency obligations that are held in the debt service reserve funds where the intent is to hold until maturity.

(Dollars in thousands)

(f) Restricted Investments by Fund

The following summarizes restricted investments as of June 30, 2014 and 2013 by various funds and accounts established by the Authority for debt covenants and other purposes:

		2014	2013
Restricted investments:			
Construction	$	80,109	129,783
Debt service reserves		224,484	229,895
Debt service		232,143	221,641
Revenue redemption		32,716	32,574
Revenue		74,128	72,195
Renewal and replacement reserve		32,182	32,793
Insurance		14,000	14,000
Community obligation and revenue enhancement		20,447	20,504
OPEB Reserve		807	805
Insurance related escrow deposits		5,192	5,308
Total restricted investments	$	716,208	759,498

(5) Bond Resolution Reserves

The components of the reserves required by the general and supplemental bond resolutions at June 30, 2014 and 2013 are as follows:

Reserves		Sewer	Water	2014 Total	2013 Total
Renewal and replacement	$	17,300	11,701	29,001	29,001
Insurance		7,000	7,000	14,000	14,000
Operating		26,369	12,603	38,972	38,802
Community obligation and revenue enhancement		18,399	1,717	20,116	20,116
Total	$	69,068	33,021	102,089	101,919

A renewal and replacement reserve of $6,000 was established through grant receipts transferred from the Commonwealth in 1985 and is included in restricted net position at June 30, 2014 and 2013.

(Dollars in thousands)

(6) Notes Payable and Long-Term Debt

Long-term debt at June 30, 2014 and 2013 consisted of the following:

		2014	2013
General Revenue Bonds:			
1993 Series C, 5 1/4%, issued December 2, 1993, due 2014 to 2015	$	19,625	28,705
2002 Series J, 5% to 5 1/2%, issued December 18, 2002, due 2014 to 2042		297,300	297,300
2006 Series A, 4% to 5%, issued March 16, 2006, due 2024 to 2046		149,990	149,990
2007 Series A, 4 3/8% to 5%, issued February 1, 2007 due 2023 to 2046		198,000	198,000
2009 Series A, 5%, issued February 19, 2009 due 2026 to 2039		76,445	80,280
2010 Series A, 3% to 5%, issued May 6, 2010 due 2018 to 2040		96,530	97,740
2011 Series B, 2% to 5%, issued May 19, 2011 due 2015 to 2041		140,140	144,840
2012 Series A, 3% to 5%, issued April 19, 2012 due 2014 to 2042		139,365	144,675
		1,117,395	1,141,530
General Revenue Refunding Bonds:			
2004 Series B, 5%, issued September 29, 2004, due 2016 to 2020		38,405	48,950
2005 Series A, 5% to 5 1/4%, issued April 14, 2005, due 2015 to 2034		344,830	344,830
2005 Series B, 5%, issued April 14, 2005, due 2031 to 2035		80,290	80,290
2006 Series B, 4% to 5%, issued March 16, 2006, due 2016 to 2040		216,935	216,935
2007 Series B, 5 1/4%, issued February 1, 2007 due 2023 to 2038		647,950	647,950
2009 Series B, 3 3/8% to 5%, issued February 19, 2009 due 2016 to 2039		271,030	274,100
2010 Series B, 5%, issued May 6, 2010 due 2014 to 2032		173,835	183,570
2011 Series C, 3 1/8% to 5 1/4%, issued December 8, 2011 due 2018 to 2042		327,160	327,160
2012 Series B, 4 1/4% to 5%, issued April 19. 2012, due 2026 to 2029		86,775	86,775
2013 Series A, 3% to 5%, issued March 27, 2013, due 2016 to 2036		169,835	170,635
		2,357,045	2,381,195

(Continued)

(Dollars in thousands)

	2014	2013
General Revenue Bonds with the Massachusetts Water Pollution Abatement Trust:		
1993 Series D, 5 1/4%, issued January 6, 1994, due 2014	$ 315	615
1995 Series A, 5% to 5 1/2%, issued November 21, 1995, due 2013 to 2015	665	1,065
1998 Series C, 4 3/4% to 5 3/8%, issued July 9, 1998, due 2013 to 2018	2,800	3,661
1999 Series E Sewer, 4 3/4% to 5 3/8%, issued October 6, 1999, due 2013 to 2029	6,984	7,305
1999 Series E Water, 4 3/4% to 5 3/8%, issued October 6, 1999, due 2013 to 2019	4,440	5,095
1999 Series F, 5 1/2% to 6%, issued November 3, 1999, due 2013 to 2029	248,850	264,940
2000 Series E Sewer, 5% to 5 5/8%, issued November 1, 2000, due 2013 to 2030	52,615	54,700
2000 Series E Water, 5% to 5 5/8%, issued November 1, 2000, due 2013 to 2020	5,400	6,070
2001 Series C Water, 5% to 5 1/4%, issued July 26, 2001, due 2015 to 2021	2,330	2,620
2001 Series D Sewer, 5 1/4% to 5 3/4%, issued July 26, 2001, due 2013 to 2029	3,438	3,874
2001 Series D Water, 5 1/4% to 5 3/4%, issued July 26, 2001, due 2013 to 2019	628	721
2002 Series H Sewer, 5% to 5 1/4%, issued October 31, 2002, due 2013 to 2032	67,935	70,420
2002 Series H Water, 5% to 5 1/4%, issued October 31, 2002, due 2013 to 2022	17,530	19,160
2002 Series I Sewer, 5% to 5 5/8%, issued October 31, 2002, due 2013 to 2030	1,890	1,970
2002 Series I Water, 5% to 5 5/8%, issued October 31, 2002, due 2013 to 2020	14	15
2003 Series A Water, 5% to 5 1/4%, issued October 31, 2002, due 2013 to 2022	806	882
2003 Series B Water, 5% to 5 1/4%, issued July 24, 2003, due 2014 to 2021	2,106	2,368
2003 Series C Sewer, 4% to 5 1/2%, issued November 6, 2003, due 2013 to 2033	24,664	25,495
2003 Series C Water, 3 3/4% to 5 1/2%, issued November 6, 2003, due 2013 to 2023	12,285	13,307

(Dollars in thousands)

		2014	2013
2004 Series C Sewer, 4% to 5 1/2%, issued October 26, 2004, due 2013 to 2033	$	8,373	8,655
2004 Series C Water, 5% to 5 1/4%, issued October 26, 2004, due 2013 to 2022		867	970
2004 Series D Sewer, 4 1/2% to 5 1/4%, issued November 29, 2004, due 2013 to 2034		45,591	47,992
2004 Series D Water, 5% to 5 1/4%, issued November 29, 2004, due 2013 to 2024		8,544	9,146
2005 Series C Sewer, 4% to 5 1/2%, issued November 3, 2005, due 2013 to 2033		5,502	5,748
2005 Series C Water, 4% to 5 1/2%, issued November 3, 2005, due 2013 to 2023		642	695
2005 Series D Sewer, 2% to 2 3/10%, issued November 16, 2005, due 2013 to 2035		51,631	53,705
2005 Series D Water, 0% to 2%, issued November 16, 2005, due 2013 to 2025		9,152	9,888
2005 Series E Sewer, 2%, issued November 16, 2005, due 2013 to 2025		263	282
2005 Series E Water, 2%, issued November 16, 2005, due 2013 to 2025		59	63
2006 Series C Sewer, 5% to 5 1/4%, issued October 26, 2006, due 2013 to 2034		6,836	7,119
2006 Series D Sewer, 2% to 2 3/10%, issued December 14, 2006, due 2013 to 2036		51,058	53,478
2006 Series D Water, 0% to 2%, issued November 16, 2006, due 2013 to 2026		19,808	21,275
2006 Series E Sewer, 2%, issued December 14, 2006, due 2013 to 2026		260	277
2006 Series E Water, 2%, issued December 14, 2006, due 2013 to 2026		116	124
2007 Series C Sewer, 2% to 2 3/10%, issued November 9, 2007, due 2013 to 2035		3,279	3,510
2007 Series C Water, 2%, issued November 9, 2007, due 2013 to 2025		1,833	1,983
2007 Series D Sewer, 2 3/10%, issued November 9, 2007, due 2013 to 2036		19,882	20,530
2007 Series E Sewer, 2% to 2 2/5%, issued December 18, 2007, due 2013 to 2037		49,807	51,752
2007 Series E Water, 2%, issued December 18, 2007, due 2013 to 2027		14,818	15,701

(Dollars in thousands)

		2014	2013
2008 Series G Sewer, 2%, issued December 9, 2008, due 2013 to 2026	$	4,374	4,680
2008 Series G Water, 2%, issued December 9, 2008, due 2013 to 2026		914	976
2009 Series C Sewer, 2% to 2 2/5%, issued March 18, 2009, due 2013 to 2038		72,808	76,666
2009 Series C Water, 2%, issued March 18, 2009, due 2013 to 2028		23,862	25,212
2009 Series D Sewer, 2% to 2 2/5%, issued December 15, 2009, due 2013 to 2037		9,386	9,802
2009 Series D Water, 2%, issued December 15, 2009, due 2013 to 2027		1,022	1,085
2010 Series D Sewer, 2% to 2 2/5%, issued July 8, 2010, due 2013 to 2040		23,954	24,764
2010 Series D Water, 2%, issued July 8, 2010, due 2013 to 2030		20,186	21,173
2011 Series A Sewer, 2% to 2 2/5%, issued March 15, 2011, due 2013 to 2038		5,204	5,458
2011 Series A Water, 2%, issued March 15, 2011, due 2013 to 2028		4,622	4,890
2012 Series C Sewer, 2% to 2 2/5%, issued June 6, 2012, due 2013 to 2040		7,342	7,701
2012 Series C Water, 2%, issued June 6, 2012, due 2013 to 2030		3,599	3,772
2012 Series D Sewer, 2% to 2 2/5%, issued June 13, 2012, due 2013 to 2042		42,229	44,049
2012 Series D Water, 2%, issued June 13, 2012, due 2013 to 2032		8,241	8,589
2013 Series B Sewer, 2% to 2 2/5%, issued May 22, 2013, due 2014 to 2043		30,476	31,947
2013 Series B Water, 2%, issued May 22, 2013, due 2014 to 2033		8,262	8,610
2014 Series C Sewer, 2% to 2 2/5%, issued May 30, 2014, due 2014 to 2042		4,911	—
2014 Series C Water, 2%, issued May 30, 2014, due 2014 to 2032		5,760	—
		1,031,168	1,076,550
General Revenue Bonds (variable rates):			
1999 Series B, 0.02% to 0.12%, issued January 29, 1999, due 2017 to 2028		58,600	62,300
		58,600	62,300

(Dollars in thousands)

		2014	2013
General Revenue Refunding Bonds (variable rates):			
2002 Series C, 0.03% to 0.22%, issued August 15, 2002, due 2020	$	35,120	35,120
2008 Series A, 0.06% to 0.24%, issued May 29, 2008, due 2014 to 2037		334,345	337,675
2008 Series C, 0.05% to 0.28%, issued May 29, 2008, due 2013 to 2026		113,840	117,680
2008 Series E, 0.05% to 0.23%, issued May 29, 2008, due 2013 to 2037		133,640	173,060
2008 Series F, 0.04% to 0.20%, issued May 29, 2008, due 2018 to 2029		50,000	164,755
2012 Series E, 0.61% to 0.78%, issued November 15, 2012, due 2016 to 2031		62,830	62,830
2012 Series F, 0.66% to 0.83%, issued November 15, 2012, due 2016 to 2031		60,300	60,300
2012 Series G, 0.76% to 0.93%, issued November 15, 2012, due 2013 to 2023		55,260	57,820
2014 Series A, 0.44% to 0.45%, issued May 20, 2014, due 2022 to 2025		50,000	—
2014 Series B, 0.58% to 0.59%, issued May 20, 2014, due 2018 to 2022		64,755	—
		960,090	1,009,240
		5,524,298	5,670,815
Less:			
Unamortized bond premiums and discounts		233,984	251,237
Current portion of long-term debt		(142,160)	(129,988)
		91,824	121,249
Long-term debt, net	$	5,616,122	5,792,064

(Dollars in thousands)

Long-term obligations at June 30, 2014 and 2013 consisted of the following:

	2014 beginning balance	Additions	Reductions	2014 ending balance	Due within one year
General revenue bonds	$ 1,203,830	—	27,835	1,175,995	20,715
General revenue refunding bonds	3,390,435	114,755	188,055	3,317,135	63,920
General revenue bonds with the Massachusetts Water Pollution Abatement trust	1,109,586	10,695	56,077	1,064,204	57,525
Borrowings associated with derivative instruments	51,594	—	2,940	48,654	—
	$ 5,755,445	125,450	274,907	5,605,988	142,160

	2013 beginning balance	Additions	Reductions	2013 ending balance	Due within one year
General revenue bonds	$ 1,273,695	—	69,865	1,203,830	19,210
General revenue refunding bonds	3,405,175	351,585	366,325	3,390,435	54,705
General revenue bonds with the Massachusetts Water Pollution Abatement trust	1,119,704	40,648	50,766	1,109,586	56,073
Borrowings associated with derivative instruments	57,392	—	5,798	51,594	—
	$ 5,855,966	392,233	492,754	5,755,445	129,988

The Authority is required to establish water and sewer rates and charges at a level sufficient to provide, among other things, primary and subordinated debt service coverage ratios of 120% and 110%, respectively. For the year ended June 30, 2014, the Authority had primary and subordinated debt service coverage ratios of 211% and 118%, respectively.

Under the Authority's General Revenue Bond Resolution, all revenues, together with the investment earnings thereon, except to the extent that such earnings are required to be deposited in the Rebate Fund pursuant to a Supplemental Resolution, are pledged for payment of the Bonds.

The Act of 1984 imposes a limitation of $600,000 on the total amount of bonds and notes which may be outstanding at any one time. The Authority has requested increases in its debt limit as necessary to allow for issuances of bonds in amounts required to finance the capital program. The state legislature increased the debt limit to $6,450,000.

On June 2, 2010, the Authority executed Bond Anticipation Notes with the Massachusetts Water Pollution Abatement Trust (MWPAT) for funding under the American Reinvestment and Recovery Act of 2009 (ARRA). The principal on these notes, totaling $33,036, will be forgiven upon issuance of a Project Completion Certificate and the Authority's compliance with the requirements of ARRA. The Authority has drawn down $33,036 to date, including $91 during Fiscal Year 2013, which is presented as long-term debt on the Authority's statements of net position.

On May 20, 2014, the Authority issued direct-purchase General Revenue Refunding Bonds, 2014 Series A and General Revenue Refunding Bonds 2014 Series B for $50,000 and $64,755, respectively. The Series A and B bonds refunded a portion of the General Revenue Refunding Bonds 2008 Series F.

The variable interest rate on these bonds will be based on 70% of LIBOR set on the first business day of each month. The monthly payment will be a combination of this variable interest and a fixed component of 34 basis points for 2014 Series A and 48 basis points for 2014 Series B.

On March 27, 2013, the Authority issued General Revenue Refunding Bonds, 2013 Series A for $170,635. The proceeds from the Series A bonds were used to refund $56,450 of General Revenue Refunding Bonds 2002 Series D, $11,835 of General Revenue Refunding Bonds 2005 Series A, $50,010 of General Revenue Bonds 2006 Series A, $47,005 of General Revenue Refunding Bonds 2006 Series B and $10,295 of General Revenue Refunding Bonds 2008 Series F.

The interest rate on these bonds is 3% to 5%. The cash flow required to make principal and interest payments on the refunding bonds is approximately $9,758 less than the debt service requirements of the refunded bonds. The economic gain (the difference between the present values of the debt service payments on the old and new debt) obtained from this refunding is $13,107.

On November 12, 2012, the Authority issued direct-purchase General Revenue Refunding Bonds, 2012 Series E, General Revenue Refunding Bonds 2012 Series F and General Revenue Refunding Bonds 2012 Series G for $62,830, $60,300 and $57,820, respectively. The Series E and F bonds refunded the General Revenue Refunding Bonds 2008 Series B in their entirety and the Series G bonds refunded a portion of the General Revenue Refunding Bonds 2008 Series C.

 (Continued)

(Dollars in thousands)

Synthetic Fixed Rate Swap Transactions

In connection with several of its bond issues, the Authority has entered into various interest rate swap agreements to reduce the impact of changes in interest rates on its variable rate debt. Under these agreements, the Authority pays a fixed interest rate (ranging from 3.9% to 6.9%) and receives interest from the swap counterparties at a variable rate (either Securities Industry and Financial Markets Association (SIFMA) rate or a percentage of LIBOR). The SIFMA rate is based on the seven-day high-grade market index of tax-exempt variable rate demand obligations.

Item	Objective	Effective date	Current notional amount	Termination date	Fixed payable swap rate	Variable receivable swap rate	Fair value at June 30, 2014	Fair value at June 30, 2013
A	Hedge changes in cash flows on the 2008 Series A Bonds	April 4, 2011	$ 133,300	August 1, 2030	5.144%	67% LIBOR	$ (9,467)	(8,781)
B	Hedge changes in cash flows on the 2008 Series E Bonds	October 28, 2008	133,300	August 1, 2030	5.494	PLUS 0.13% SIFMA	(17,485)	(17,085)
C	Hedge changes in cash flows on the 2008 Series A and E Bonds	August 1, 2030	70,400	August 1, 2037	6.585	67% LIBOR	(1,079)	(829)
D	Hedge changes in cash flows on the 2008 Series C Bonds	May 29, 2008	101,155	November 1, 2026	3.994	PLUS 0.13% SIFMA	(10,709)	(11,665)
E	Hedge changes in cash flows on the 2008 Series C and 2012 Series G Bonds	May 29, 2008	67,440	November 1, 2026	4.033	SIFMA	(185)	193
F	Hedge changes in cash flows on the 2008 Series A and E Bonds	August 15, 2002	99,245	August 1, 2015	4.127	67% LIBOR	(2,052)	(5,700)
						Total	$ (40,977)	(43,867)

All of the above are pay-fixed interest rate swap agreements. Under these interest rate swap agreements, the Authority incurred net interest expense of $24,364 and $23,591 in Fiscal Year 2014 and Fiscal Year 2013, respectively.

For the swap execution on April 4, 2011, with a current notional amount of $133,300, the fixed rate paid by the Authority is as follows: 4.120% from execution through August 2013, 5.144% from August 2013 through August 2019, and 6.585% from, August 2019 through August 2030.

For the swap execution on October 28, 2008, with a current notional amount of $133,300, the fixed rate paid by the Authority is as follows: 4.470% from execution through August 2013, 5.494% from August 2013 through August 2019, and 6.935% from August 2019 through August 2030.

The aggregate fair value balance of the derivative instruments at June 30, 2014 and 2013 is $(40,977) and $(43,867), respectively, and is reflected on the Authority's statements of net position as a liability for derivative instruments. This liability is offset by deferred outflows from derivative instruments. The original notional amounts of the interest rate swaps totaled $885,895.

The fair values of the interest rate swaps were estimated using the zero-coupon method. This method calculates the future net settlement payments required by the swap, assuming that the current forward rates implied by the yield curve correctly anticipate future spot interest rates. These payments are then discounted using the spot rates implied by the current yield curve for hypothetical zero-coupon bonds due on the date of each future net settlement on the swaps.

Risk Disclosure

Credit Risk – Because all of the Authority's swaps rely upon the performance of the third parties who serve as swap counterparties, the Authority is exposed to credit risk, or the risk that a swap counterparty fails to perform according to its contractual obligations. The appropriate measurement of this risk at the reporting date is the fair value of the swaps, as shown in the columns labeled Fair Value in the tables above. To mitigate credit risk, the Authority maintains strict credit standards for swap counterparties. The Authority monitors swap counterparties' credit ratings by the three rating agencies (FitchRatings, Moody's Investors Service, and Standard and Poor's). Collateral may be obtained from any counterparty that does not maintain a set credit rating. Since all derivatives are in a liability position, there is no amount exposed to credit risk.

The following represents the credit ratings of the counterparties as of June 30, 2014:

Derivative instrument	Counterparty credit rating
Derivative A	A
Derivative B	AA-
Derivative C	A
Derivative D	A
Derivative E	A
Derivative F	A

Basis Risk – The Authority is exposed to basis risk because the floating index the Authority receives on the swaps (SIFMA or 67% of LIBOR) may be different than the basis of the variable rate on the associated bonds. Should this occur, the expected savings may not be realized.

Termination Risk – The Authority or its counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract. If, at the time of termination, a derivative is in a liability position, the Authority would be liable to the counterparty for a payment equal to the liability, subject to netting arrangements.

Rollover Risk – The Authority can be exposed to rollover risk on hedging derivative instruments that are hedges of debt that terminate prior to the maturity of the debt. The Authority currently has no rollover risk. When Derivative instruments A and B terminate in 2030, those bond series will then be hedged by Derivative instrument C.

Swap Payments and Associated Bonds Outstanding

Bonds outstanding include certain variable rate bonds where the Authority pays a fixed interest rate and receives interest at a variable rate from the counterparty. The table below presents the debt service requirements and related net swap payments for these bonds. As rates vary, variable rate interest payments will vary.

(Dollars in thousands)

Using rates as of June 30, 2014, debt service requirements of the hedged variable rate bonds and net swap payments, assuming current interest rates remain constant, were as follows:

	Variable-rate Principal	Variable-rate Interest	Interest rate swaps, net	Total
Fiscal year ending June 30:				
2015	$ 55,235	277	23,041	78,553
2016	57,710	247	19,653	77,610
2017	7,197	241	15,845	23,283
2018	25,003	237	12,681	37,921
2019	26,000	223	10,286	36,509
2020–2024	212,000	656	41,014	253,670
2025–2029	80,895	273	16,768	97,936
2030–2034	16,800	175	12,575	29,550
2035–2039	53,600	46	4,459	58,105
Total	$ 534,440	2,375	156,322	693,137

At June 30, 2014, the following bonds outstanding are considered defeased in-substance:

Description	Redemption date	Redemption price	Outstanding principal amount
1992 Series A	2014–2019	100	$ 240,910
1993 Series C	2014–2015	100	30,690
1997 Series D	2014	100	7,310
1998 Series A	2014	100	5,745
1998 Series B	2014–2016	100	13,865
2002 Series J	2015	100	9,075
2004 Series A	2014	100	118,215
2004 Series B	2014	100	26,850
2005 Series A	2014, 2017	100	26,760
2006 Series A	2016, 2018	100	50,010
2006 Series B	2015–2018	100	69,385
2007 Series A	2017	100	2,000
2009 Series A	2014–2016	100	11,175
2009 Series B	2014–2015	100	5,760
2010 Series A	2015–2017	100	3,470
2010 Series B	2017	100	9,735
2011 Series B	2014, 2017	100	4,770
2012 Series A	2015–2017	100	8,150
2013 Series A	2017	100	800

(Dollars in thousands)

The proceeds and available funds were deposited in irrevocable trusts with escrow agents in an amount which will provide for payment of interest due to the redemption date and redemption of the defeased bonds outstanding on such date. The defeased portion of such debt, accrued interest thereon, and related unamortized issuance and discount costs were removed from the statements of net position in an in substance defeasance transaction.

In June 2014, the Authority used funds on hand to defease $1,210 of the 2010 Series A, $2,105 of the 2011 Series B and $2,825 of the 2012 Series A General Revenue bonds outstanding and $10,545 of the 2004 Series B and $9,735 of the 2010 Series B and $800 of the 2013 Series A General Revenue Refunding bonds outstanding.

In June 2013, the Authority used funds on hand to defease $7,180 of the 2009 Series A, $1,155 of the 2010 Series A and $5,325 of the 2012 Series A General Revenue bonds outstanding and $3,120 of the 2009 Series B General Revenue Refunding bonds outstanding.

At June 30, 2014, outstanding bonds that are redeemable before their scheduled due dates are as follows:

Description	Redemption date	Redemption price	Outstanding principal amount
2002 Series J	on or after August 1, 2012	100	$ 1,000
2004 Series B	December 2014	100	38,405
2005 Series A	August 2017	100	273,155
2005 Series B	August 2017	100	80,290
2006 Series A	August 2018	100	14,895
2006 Series A	August 2016	100	135,095
2006 Series B	August 2018	100	76,330
2006 Series B	August 2016	100	138,440
2007 Series A	February 2017	100	198,000
2009 Series A	August 2019	100	76,445
2009 Series B	August 2019	100	181,885
2010 Series A	August 2020	100	92,545
2010 Series B	August 2020	100	114,565
2011 Series B	August 2021	100	120,385
2011 Series C	August 2016	100	6,000
2011 Series C	August 2021	100	291,160
2012 Series A	August 2016	100	6,440
2012 Series A	August 2022	100	120,740
2012 Series B	August 2022	100	86,775
2013 Series A	August 2023	100	46,515

The variable rate General Revenue Bonds are subject to redemption prior to maturity at the option of the Authority in whole or in part, on any interest payment date for bond Series 1999B and 2002C and D and on any business day for bond Series 2008A, 2008C through F, 2012G, 2014A and 2014B, respectively. Series 2012E and 2012F are subject to redemption prior to maturity on any interest payment date after November 15, 2014 and November 3, 2014, respectively.

(Dollars in thousands)

During Fiscal Year 2014, the Authority executed loan agreements with the MWPAT providing for 2014 Series C Sewer and Water loans in the principal amounts of $4,911 and $5,760 respectively. All proceeds for these loans were received by June 30, 2014.

During Fiscal Year 2013, the Authority executed loan agreements with the MWPAT providing for 2013 Series B Sewer and Water loans in the principal amounts of $31,947 and $8,610 respectively. All proceeds for these loans were received by June 30, 2013.

Federal and Commonwealth subsidies for purposes of offsetting principal payments aggregating $54,076 will be recognized as capital grants in aid of construction over the term of the loans.

Interest is payable semiannually on all debt, except on the commercial paper, on which interest is payable upon maturity and the General Revenue Bonds with variable interest rates on which interest is payable monthly. The Senior General Revenue Bonds and the General Revenue Refunding Bonds are collateralized equally and ratably by a lien and pledge on substantially all of the Authority's cash and revenues, except the operating fund. The subordinated debt series, including the commercial paper are collateralized equally and ratably by a subordinated pledge on substantially all of the Authority's revenues and cash and investments, except the operating, senior debt service, and debt service reserve funds. Premiums, discounts, issuance costs, and the excess of reacquisition price over the carrying amount of the defeased debt are being amortized over the lives of the respective issues.

The amounts of long-term debt, principal, and interest payable in future fiscal years are as follows:

	Principal	Interest	Total
Year ending June 30:			
2015	$ 142,160	233,854	376,014
2016	163,732	227,343	391,075
2017	176,449	221,810	398,259
2018	227,476	213,105	440,581
2019	235,433	203,058	438,491
2020–2024	1,467,771	852,290	2,320,061
2025–2029	1,299,578	549,717	1,849,295
2030–2034	844,498	312,641	1,157,139
2035–2039	603,002	149,619	752,621
2040–2044	283,014	43,459	326,473
2045–2049	81,185	5,287	86,472
Total	$ 5,524,298	3,012,183	8,536,481

The Authority issued commercial paper notes of $170,000 to finance capital expenditures, which are secured by $100,000 and $250,000 irrevocable direct-pay letters of credit which expire on September 8, 2015, and November 30, 2015, respectively. These letters of credit carry a fee of 0.65% and 0.30% per annum, respectively, on the amount available. The maximum aggregate principal amount of commercial paper which may be outstanding at any one time is $350,000.

(Dollars in thousands)

Commercial paper at June 30, 2014 and 2013 consisted of the following:

	2014 Beginning balance	Additions	Reductions	2014 Ending balance
0.21% commercial paper	$ —	34,000	—	34,000
0.31% commercial paper	—	87,000	—	87,000
0.17% commercial paper	—	49,000	—	49,000
0.32% commercial paper	34,000	—	34,000	—
0.35% commercial paper	87,000	—	87,000	—
0.17% commercial paper	23,000	—	23,000	—
	$ 144,000	170,000	144,000	170,000

	2013 Beginning balance	Additions	Reductions	2013 Ending balance
0.32% commercial paper	$ 34,000	—	—	34,000
0.35% commercial paper	87,000	—	—	87,000
0.17% commercial paper	—	23,000	—	23,000
0.29% commercial paper	23,000	—	23,000	—
	$ 144,000	23,000	23,000	144,000

(7) Accounts Receivable/Intergovernmental Loans

The Authority has entered into various interest-free loan agreements with certain member communities. Under these agreements, the Authority loaned these communities $29,531 and $52,389 in Fiscal Year 2014 and 2013, respectively, to be received in five or ten equal annual installments.

The long-term portion of these loans at June 30, 2014 and 2013, is $125,439 and $126,212, respectively, and is included in other assets. The loans due within one year total $30,304 and $29,768 at June 30, 2014 and 2013, respectively. This program is designed to assist member communities with sewer and water systems rehabilitation.

(Dollars in thousands)

(8) Capital Assets

Capital assets at June 30, 2014 and 2013 consisted of the following:

	2013	Additions	Disposals/ transfers	2014
Capital assets – not being depreciated:				
Land	$ 23,733	8	—	23,741
Construction in progress	163,916	95,499	(66,235)	193,180
Total capital assets – not being depreciated	187,649	95,507	(66,235)	216,921
Capital assets – being depreciated:				
Plant and equipment – water and sewage system	8,974,445	64,897	—	9,039,342
Furniture and fixtures	17,177	—	—	17,177
Leasehold improvements	2,423	—	—	2,423
Motor vehicles and equipment	3,100	1,330	—	4,430
Total capital assets – being depreciated	8,997,145	66,227	—	9,063,372
Less accumulated depreciation for:				
Plant and equipment – water and sewage system	3,011,587	175,670	—	3,187,257
Furniture and fixtures	16,427	325	—	16,752
Leasehold improvements	2,084	12	—	2,096
Motor vehicles and equipment	770	279	—	1,049
Total accumulated depreciation	3,030,868	176,286	—	3,207,154
Total capital assets – being depreciated – net	5,966,277	(110,059)	—	5,856,218
Capital assets – net	$ 6,153,926	(14,552)	(66,235)	6,073,139

(Continued)

(Dollars in thousands)

Capital assets at June 30, 2013 and 2012 consisted of the following:

		2012	Additions	Disposals/ transfers	2013
Capital assets – not being depreciated:					
Land	$	24,255	—	(522)	23,733
Construction in progress		159,878	96,237	(92,199)	163,916
Total capital assets – not being depreciated		184,133	96,237	(92,721)	187,649
Capital assets – being depreciated:					
Plant and equipment – water and sewage system		8,882,812	91,633	—	8,974,445
Furniture and fixtures		17,136	41	—	17,177
Leasehold improvements		2,423	—	—	2,423
Motor vehicles and equipment		2,339	761	—	3,100
Total capital assets – being depreciated		8,904,710	92,435	—	8,997,145
Less accumulated depreciation for:					
Plant and equipment – water and sewage system		2,837,669	173,918	—	3,011,587
Furniture and fixtures		16,103	324	—	16,427
Leasehold improvements		2,072	12	—	2,084
Motor vehicles and equipment		605	165	—	770
Total accumulated depreciation		2,856,449	174,419	—	3,030,868
Total capital assets – being depreciated – net		6,048,261	(81,984)	—	5,966,277
Capital assets – net	$	6,232,394	14,253	(92,721)	6,153,926

Depreciation and amortization for Fiscal Years 2014 and 2013 was $193,062 and $190,852, respectively.

(Continued)

(Dollars in thousands)

(9) Leases

(a) Operating

The Authority leases electrical power assets, office space in Boston, and other property under long-term operating leases. Future minimum rental payments required under operating leases having initial or remaining noncancelable lease terms in excess of one year at June 30, 2014 are as follows:

Year ending June 30:		
2015	$	4,654
2016		3,335
2017		3,094
2018		3,148
2019		3,195
2020–2024		11,381
Total	$	28,807

Rental expense was $6,970 and $7,133 in Fiscal Years 2014 and 2013, respectively.

(b) Capital

In Fiscal Year 2003, the Authority entered into a 30-year capital lease agreement for the new maintenance facility. The interest rate for the capital lease is 7.83%. Future minimum lease payments for the capital lease at June 30, 2014 are as follows:

		Principal	Interest	Total
Year ending June 30:				
2015	$	824	2,393	3,217
2016		891	2,326	3,217
2017		963	2,254	3,217
2018		1,041	2,176	3,217
2019		1,126	2,091	3,217
2020–2024		7,156	8,929	16,085
2025–2029		10,572	5,513	16,085
2030–2034		8,365	1,019	9,384
Total	$	30,938	26,701	57,639

Under this lease, the Authority is also responsible for “Additional Rent,” as defined in the lease. The Additional Rent includes real estate taxes, assessments, and other government charges.

The associated capital asset is reported in plant and equipment – water and sewage system at a cost of $37,134 with $14,855 of accumulated depreciation as of June 30, 2014.

(10) Retirement Benefits

(a) Plan Description

The Enabling Act provided for the establishment of the Massachusetts Water Resources Authority Employees' Retirement System (the Plan), a contributory single-employer retirement system that is separate from the State Employees Retirement System. The Plan is a defined benefit pension plan covering those employees not employed by the MDC prior to July 1, 1985. Covered payroll for all Authority employees in the Plan was $84,829 at the actuarial valuation date, January 1, 2013.

Under the provisions of the Plan, pension benefits vest after 10 years of full-time employment. An employee may retire after 20 years of service or at age 55 and completion of 10 years of service. At age 65, annual pension benefits equal 2.5% of the employee's average regular compensation earned during the last three years of employment or any three consecutive years when compensation was higher, multiplied by each year of creditable service. The benefit is reduced if retirement occurs before age 65 or if survivor's benefits are elected. The Plan also provides death and disability benefits. Ordinary disability benefits are available only to employees under age 55 with at least 10 years of service. Complete financial statements for the Plan can be obtained from the Authority's administrative offices at Charlestown Navy Yard, 100 First Avenue, Boston, MA 02129.

(b) Funding Policy

Contributions made by employees are based upon a percentage of employee base pay (5% for employees hired on or before December 31, 1974, 7% for employees hired between January 1, 1975 and December 31, 1983, 8% for employees hired between January 1, 1984, and June 30, 1996, and 9% for employees hired on or after July 1, 1996). Additionally, certain employees earning in excess of $30 contribute an extra 2% of their salary effective January 1, 1979. Employees receive full payment of contributions upon withdrawal from the Plan and 50% of interest earned for employees with five to nine years of service or 100% of interest earned for employees with 10 or more years of service.

The Authority's 2014 and 2013 contributions to the plan were based on an amount approved by the Retirement Board and the Authority's board of directors, which is based on an actuarially determined amount. The Authority's Enabling Act requires funding to be made in accordance with the Retirement Board's recommendation.

(Dollars in thousands)

(c) ***Annual Pension Cost and Net Pension Obligation***

The annual required contribution for the year ended June 30, 2014, determined by the January 1, 2011 actuarial valuation, was as follows:

Annual required contribution	$	5,903
Contributions made		(5,903)
Increase (decrease) in net pension obligation		—
Net pension obligation, beginning of year		—
Net pension obligation, end of year	$	—

(d) ***Three-Year Trend Information***

		Annual pension cost (APC)	Percentage of ARC contributed		Net pension asset (obligation)
Fiscal year ending:					
2014	$	5,903	100%	$	—
2013		5,750	100		—
2012		5,489	100		—

(e) ***Funded Status and Funding Progress***

As of January 1, 2013, the most recent actuarial valuation date, the funded status of the Plan was as follows:

Actuarial accrued liability	$	385,296
Actuarial value of assets		341,515
Unfunded actuarial accrued liability (UAAL)	$	43,781
Funded ratio		88.6%
Covered payroll	$	84,829
UAAL as percentage of covered payroll		51.6%

The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the actuarial value of plan assets are increasing or decreasing over time relative to the actuarial accrued liability for benefits. Effective for the January 1, 2007 actuarial valuation, the Authority changed to the entry age normal actuarial cost method. Prior actuarial valuations were completed using the aggregate cost method.

(f) Actuarial Methods and Assumptions

The annual required contribution for the current year was determined as part of the January 1, 2011, actuarial valuation using the entry age normal actuarial cost method. Under this method an unfunded actuarial accrued liability of $42,190 was calculated. The actuarial assumptions included (a) 8% investment rate of return and (b) projected salary increase of 4.75% per year. Liabilities for cost of living increases have been assumed at an annual increase of 3%, on the first $12 of benefit payments. The actuarial value of assets is determined by projecting the market value of assets as of the beginning of the prior plan year with the assumed rate of return during that year (8.0%) and accounting for deposits and disbursements with interest at the assumed rate of return. An adjustment is then applied to recognize the difference between the actual investment return and expected return over a five year period. As of January 1, 2011 the unfunded actuarially accrued liability is being amortized over 13 years using an open group method which assumes a 4.5% per year increase in payroll.

(g) Other Benefits

All MDC personnel who became employees of the Authority on July 1, 1985, and were members of the State Employees Retirement System, retained their membership in that system. The Authority is not liable for retirement allowances paid to or on account of these employees. Funding of the pension liability of the State Employees Retirement System is the obligation of the Commonwealth. Employees covered by this plan become 100% vested after 10 years of service.

(11) Other Postemployment Benefits (OPEB)

(a) Plan Description

In addition to providing the pension benefits described, the Authority provides postemployment health care and life insurance benefits for retired employees through the Group Insurance Commission (GIC). The GIC is a quasi-independent state agency that administers an agent multi-employer defined benefit OPEB plan. The benefits, benefit levels, employee contributions and employer contributions are governed by the Authority and can be amended by the Authority. As of January 1, 2012, the actuarial valuation date, approximately 478 retirees and survivors and 1,149 active employees meet the eligibility requirements. The plan does not issue a separate financial report.

(b) Benefits Provided

The Authority provides medical, prescription drug, mental health/substance abuse and life insurance to retirees and their covered dependents. All active employees who retire from the Authority and meet the eligibility criteria will receive these benefits.

(Dollars in thousands)

(c) *Funding Policy*

Retirees who retired on or before July 1, 1994 contribute 10% of the cost of the health plans, as determined by the GIC. Those who retired after July 1, 1994 contribute 15% of the cost of the health plan and those who retired after October 1, 2009 contribute 20% of the cost of the health plan, as determined by the GIC. The Authority contributes the remainder of the health plan costs on a pay-as-you-go basis.

(d) *Annual OPEB Costs and Net OPEB Obligation*

The Authority's Fiscal Year 2014 annual OPEB expense is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost per year and amortize the unfunded actuarial liability over a period of thirty years. The following table shows the components of the Authority's annual OPEB cost for the year ending June 30, 2014, the amount actually contributed to the plan, and the change in the Authority's net OPEB obligation based on an actuarial valuation as of January 1, 2012:

Annual Required Contribution (ARC)	$	16,956
Interest on net OPEB obligation		3,761
Adjustment to ARC		(3,481)
Annual OPEB cost		17,236
Contributions made		(3,715)
Increase in net OPEB obligation		13,521
Net OPEB obligation – beginning of year		88,482
Net OPEB obligation – end of year	$	102,003

The Authority's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation were as follows:

Fiscal year ended		Annual OPEB cost	Percentage of OPEB cost contributed		Net OPEB obligation
2014	$	17,236	22%	$	102,003
2013		16,044	18		88,482
2012		19,104	21		75,360

(Dollars in thousands)

(e) Funded Status and Funding Progress

The funded status of the plan as of January 1, 2012, the date of the most recent actuarial valuation, was as follows:

Actuarial accrued liability (AAL)	$	197,191
Actuarial value of plan assets		—
Unfunded actuarial accrued liability (UAAL)	$	197,191
Funded ratio (actuarial value of plan assets/AAL)		—%
Covered payroll (active plan members)	$	82,679
UAAL as a percentage of covered payroll		238.5%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amount and assumptions about the probability of occurrence of events far into the future. Examples included assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

(f) Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the plan as understood by the Authority and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the Authority and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2012 actuarial valuation the projected unit credit cost method was used. The actuarial value of assets was not determined as the Authority has not advance funded its obligation. The actuarial assumptions included a 4.25% investment rate of return and an initial annual healthcare cost trend rate of 9.5% which decreases to a 5.5% long-term trend rate for all healthcare benefits after ten years. The amortization costs for the initial UAAL is a level percentage of payroll for a period of 30 years, on a closed basis. This has been calculated assuming the amortization payment increases at a rate of 3.25%.

(12) Commitments and Contingencies

(a) General

The Authority's capital improvement program continues to proceed. As part of this program, the Authority has entered into a number of contracts for the design and construction of infrastructure and improvements to its facilities. Commitments under these contracts aggregated approximately $357,424 at June 30, 2014.

The Authority's operating and construction plans are designed to comply with the Federal District Court's schedule of actions. The Authority has incurred capital expenditures of approximately $10,430,000 from Fiscal Years 1986 through 2014, including those projects required to comply with the Federal District Court's schedule. The Authority anticipates spending an additional $1,926,000 on these projects through Fiscal Year 2023. These capital expenditures have been forecasted based upon certain preliminary assumptions and estimates, which may change significantly as design and construction of the necessary facilities proceed. Funding is expected to come from various federal and state grants, as available and approved, and from the Authority's debt proceeds. To date, federal appropriations for the Boston Harbor Project have aggregated $810,000.

(b) Boston Harbor Case

The Authority continues to be a defendant, along with Boston Water and Sewer Commission (BWSC) and the Commonwealth, in the federal Boston Harbor Case. The federal action was originally brought in 1985 by the United States on behalf of the United States Environmental Protection Agency (EPA) and by certain citizens groups for Clean Water Act violations. As part of the Boston Harbor Case, the Authority was required to undertake certain corrective actions to meet wastewater treatment, discharge and combined sewer overflow (CSO) requirements. The only corrective action remaining is CSO related which is currently scheduled for completion in 2015.

In March 2006, the Authority reached agreement with the United States and the Massachusetts Department of Environmental Protection (DEP) on the scope and schedule for the remaining CSO projects which was filed with the Court as part of a joint motion to amend the Court Schedule. In April 2006, the Court allowed the joint motion and issued an Order with a schedule. Under the Order, the Authority has until 2020 to complete the remaining CSO work and subsequent monitoring which will be used to verify that the long term CSO control goals are achieved.

As part of the agreement, DEP agreed to reissue and EPA agreed to approve five (5) consecutive variances of no more than three years duration each, through the year 2020, for the Charles River and Alewife Brook/Upper Mystic River that are consistent with and limited to the requirements in the Authority's revised Long Term CSO Control Plan. Variances have most recently been issued by DEP in or about August 2013. The variances will respectively remain in place for the Charles River until October 1, 2016 and for the Alewife/Upper Mystic until September 1, 2016. In addition, the United States and the Authority agreed to withdraw the February 27, 1987 *Stipulation of the United States and the Massachusetts Water Resources Authority on Responsibility and Legal Liability for Combined Sewer Overflows* and replace it with a Second Stipulation that requires the Authority to implement the CSO requirements set forth in the Court Schedule and to meet the levels of control described in the Authority's long term CSO control plan. Upon completion of the long term CSO control plan and with results that demonstrate performance parameters are as predicted, the stipulation makes the Authority responsible for only those CSO outfalls which it owns and operates. As a result of the agreement, the Authority now has 35 CSO projects, of which, 32 are complete and two are under construction. The final project construction contract has been awarded the project is expected to commence in the Fall of 2014.

December 2015 is the scheduled completion date for the last of the CSO projects. The federal court schedule requires MWRA to commence a three-year performance assessment of the completed projects starting in January 2018 and to submit a report to the Court assessing attainment of the long term control levels by December 2020.

There has been no imposition of penalties by the Court against MWRA on the merits of the claims originally asserted in the Boston Harbor Case to date. The Court always retains the right to order remedial action and to assess penalties.

(c) Deer Island Submarine Power Cable

In 2004, the United States Army Corps of Engineers (Corps) asserted that Boston Edison Co. (NStar), its subsidiary Harbor Energy Electric Company (HEEC), and the Authority were in violation of a permit (MA BOSS 198900530, dated August 31, 1989) which authorized the installation of a submarine electric power cable. The cable runs under the channel bed of Boston Harbor and extends from South Boston to Deer Island and is used to provide electric power for Deer Island operations. The Corps alleges that the power cable, in places, has been installed at depths less than those required by the permit. The Corps has demanded that the permittees develop plans and an implementation schedule for bringing the cable's depth and location into compliance with the permit. The demand has been made in connection with and in anticipation of a Massachusetts Port Authority project known as the Boston Harbor Deep Draft Navigation Improvement Project. The Project involves dredging operations intended to deepen the harbor channel so as to make it navigable by deep-draft vessels. The intended route of the Project's dredging operations will come very close to the depth at which the cable is believed to be located. The Project has now received the various design, environmental and state and federal funding approvals necessary to the start of the work. Project dredging operations in the vicinity of the cable could begin within one year's time.

The Authority has responded to the Corps stating that it had become a co-permittee only to facilitate issuance of the permit, that it did not install and has never owned the cable, and therefore, it has neither any right nor financial responsibility, nor the ability, to move or alter the position of the cable. In May 2005, the Department of Justice (DOJ) advised the permittees that the matter had been referred to DOJ by the Corps for the purpose of either commencing a lawsuit to compel the relocation of the cable or negotiating an amicable resolution that would bring the permittees into compliance with the permit's conditions. The Authority has informed the Court in the Boston Harbor Case of its position in its Compliance and Progress report filed on June 15, 2005. Discussions among the interested parties over the years has produced a method proposed and intended by NSTAR and HEEC for protection of the cable from the Massport project by way of carefully exposing it and placing concrete mats over it, without either moving it or burying it deeper in the channel. The Authority has advised NSTAR and HEEC that it has no financial responsibility whatsoever for the costs of either protecting or relocating the cable.

(d) Miscellaneous

The Authority is also a defendant in several legal actions and administrative proceedings arising out of its operation, maintenance, and improvement of the water and sewer systems under its care. It is the opinion of management that any judgments or settlements that may result from these actions will not have a materially adverse effect upon the Authority.

(13) Risk Management

The Authority is exposed to various risks of loss. The risk management program involves insurance and self insurance related to property, general liability (including automobile, marine and employers' liability), excess liability, public officials' liability, workers' compensation, unemployment liability, and employee health care and life insurance.

Buildings, plants, and equipment are fully insured on an all risk replacement basis to the extent that losses exceed $2,500 per occurrence. The Authority maintains insurance coverage for general liability, automobile liability, marine liability, and employers' liability to the extent that losses exceed $2,500 per occurrence, up to a limit of $25,000. In addition to the primary liability insurance, the Authority maintains excess liability policies with additional limits of $75,000. The Authority also maintains public officials' errors and omissions insurance with a limit of $5,000 per occurrence with a $1,000 deductible. All insurance policies are renewed on an annual basis

REQUIRED SUPPLEMENTARY INFORMATION

MASSACHUSETTS WATER RESOURCES AUTHORITY

Schedules of Funding Progress

Required Supplementary Information

June 30, 2014

(Unaudited)

(Dollars in thousands)

Employees' retirement system

Actuarial valuation		Assets (a)	Actuarial Accrued Liability (AAL) – (b)	Unfunded AAL (UAAL) (b-a)	Funded ratio (a/b)		Covered payroll (c)	UAAL as a percentage of covered payroll ((b-a)/(c))
January 1, 2013	$	341,515	385,296	43,781	88.6	$	84,829	51.6
January 1, 2011		299,331	341,521	42,190	87.6		82,870	50.9
January 1, 2010		276,270	319,876	43,606	86.4		81,962	53.2
January 1, 2009		222,477	301,652	79,175	73.8		82,314	96.2
January 1, 2008		240,484	278,050	37,566	86.5		78,925	47.6
January 1, 2007		211,716	255,962	44,246	82.7		75,444	58.6

Effective for the January 1, 2007 actuarial valuation, the Authority changed actuarial cost methods. See footnote 10 (e).

Other postemployment benefits

Actuarial valuation		Assets (a)	Actuarial Accrued Liability (AAL) – (b)	Unfunded AAL (UAAL) (b-a)	Funded ratio (a/b)		Covered payroll (c)	UAAL as a percentage of covered payroll ((b-a)/(c))
January 1, 2012	$	—	197,191	197,191	—	$	82,679	238.5
January 1, 2010		—	192,096	192,096	—		81,372	236.1
January 1, 2008		—	180,833	180,833	—		79,298	228.0
January 1, 2006		—	154,449	154,449	—		72,476	213.1

See accompanying independent auditors' report.

SUPPLEMENTAL SCHEDULES

MASSACHUSETTS WATER RESOURCES AUTHORITY

Accounts Established by the General Revenue Bond Resolution

Year ended June 30, 2014
(comparative totals for June 30, 2013)

(Dollars in thousands)

		Construction	Revenue	Debt service	Reserves	Total
Balance – June 30, 2013	$	129,783	72,195	504,614	46,793	753,385
Proceeds from:						
Revenue bonds and loans		36,571	—	114,575	—	151,146
Cash received from customers		—	647,592	—	—	647,592
Interest income		163	3,400	3,142	(578)	6,127
Debt service grant		—	—	854	—	854
Grant receipts		293	—	5,665	—	5,958
Construction payments		(92,807)	—	—	—	(92,807)
Capital lease payments		(765)	—	(2,452)	—	(3,217)
Debt service payment		(2,155)	(29,196)	(471,585)	—	(502,936)
Other commonwealth payments		—	(26,284)	—	—	(26,284)
Interfund transfers		8,143	(360,621)	352,511	(33)	—
Transfers from (to) operating account		883	(232,958)	2,466	—	(229,609)
Balance – June 30, 2014	$	80,109	74,128	509,790	46,182	710,209

		Sewer	Water	2014 total	2013 total
Restricted investments:					
Construction	$	61,337	18,772	80,109	129,783
Debt service reserves		145,428	79,056	224,484	229,895
Debt service		171,129	61,014	232,143	221,641
Revenue redemption		5,783	26,933	32,716	32,574
Revenue		9,860	64,268	74,128	72,195
Renewal and replacement reserve		20,726	11,456	32,182	32,793
Insurance		7,000	7,000	14,000	14,000
Community obligation and revenue enhancement		12,823	7,624	20,447	20,504
Total restricted investments	$	434,086	276,123	710,209	753,385

See accompanying independent auditors' report.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Combining Statement of Net Position

June 30, 2014

(Dollars in thousands)

Assets	**Sewer**	**Water**	**Combined total**
Unrestricted current assets:			
Cash and cash equivalents	$ 35,469	22,019	57,488
Investments	26,117	11,652	37,769
Intergovernmental loans	8,634	21,670	30,304
Accounts receivable	99	907	1,006
Total unrestricted current assets	70,319	56,248	126,567
Restricted assets:			
Investments	438,143	278,065	716,208
Interest receivable	1,441	1,101	2,542
Total restricted assets	439,584	279,166	718,750
Capital assets:			
Capital assets – not being depreciated	142,791	74,130	216,921
Capital assets – being depreciated – net	3,493,338	2,362,880	5,856,218
Total capital assets	3,636,129	2,437,010	6,073,139
Regulatory assets	627,931	169,660	797,591
Other assets – net	272,532	127,188	399,720
Total assets	5,046,495	3,069,272	8,115,767
Deferred Outflows of Resources			
Deferred outflows from derivative instruments	37,282	3,695	40,977
Deferred outflows from refunding debt	42,846	30,771	73,617
Liabilities			
Current liabilities:			
Accounts payable and accrued expenses	48,476	10,958	59,434
Commercial paper notes	92,000	78,000	170,000
Current portion of long-term debt	116,250	25,910	142,160
Total current liabilities	256,726	114,868	371,594
Payable from restricted assets:			
Accounts payable for construction	23,267	5,368	28,635
Accrued interest on bonds payable	56,307	30,676	86,983
Reserves	69,068	33,021	102,089
Total payable from restricted assets	148,642	69,065	217,707
Retainage on construction in progress	2,496	3,327	5,823
Long-term debt – less current portion	3,690,335	2,007,477	5,697,812
Long-term capital leases	21,213	9,725	30,938
Other postemployment benefits	71,890	30,113	102,003
Liability for derivative instruments	37,282	3,695	40,977
Total liabilities	4,228,584	2,238,270	6,466,854
Deferred Inflows of Resources			
Deferred inflows from regulated activities	(21,297)	28,389	7,092
Net Position			
Net investment in capital assets	201,738	572,652	774,390
Restricted	189,572	81,852	271,424
Unrestricted	528,026	182,575	710,601
Total net position	$ 919,336	837,079	1,756,415
Commitments and contingencies			

See accompanying independent auditors' report.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Combining Statement of Net Position

June 30, 2013

(Dollars in thousands)

Assets	Sewer	Water	Combined total
Unrestricted current assets:			
Cash and cash equivalents	$ 28,346	17,615	45,961
Investments	33,839	14,980	48,819
Intergovernmental loans	8,505	21,263	29,768
Accounts receivable	75	536	611
Total unrestricted current assets	70,765	54,394	125,159
Restricted assets:			
Investments	476,452	283,046	759,498
Interest receivable	2,065	1,388	3,453
Total restricted assets	478,517	284,434	762,951
Capital assets:			
Capital assets – not being depreciated	106,687	80,962	187,649
Capital assets – being depreciated – net	3,596,390	2,369,887	5,966,277
Total capital assets	3,703,077	2,450,849	6,153,926
Regulatory assets	648,991	169,689	818,680
Other assets – net	285,330	124,996	410,326
Total assets	5,186,680	3,084,362	8,271,042
Deferred Outflows of Resources			
Deferred outflows from derivative instruments	39,727	4,140	43,867
Deferred outflows from refunding debt	50,909	36,451	87,360
Liabilities			
Current liabilities:			
Accounts payable and accrued expenses	45,225	9,624	54,849
Commercial paper notes	92,000	52,000	144,000
Current portion of long-term debt	107,396	22,592	129,988
Total current liabilities	244,621	84,216	328,837
Payable from restricted assets:			
Accounts payable for construction	10,113	6,910	17,023
Accrued interest on bonds payable	55,817	30,146	85,963
Reserves	69,272	32,647	101,919
Total payable from restricted assets	135,202	69,703	204,905
Retainage on construction in progress	2,293	5,780	8,073
Long-term debt – less current portion	3,834,460	2,042,235	5,876,695
Long-term capital leases	21,685	10,015	31,700
Other postemployment benefits	62,561	25,921	88,482
Liability for derivative instruments	39,727	4,140	43,867
Total liabilities	4,340,549	2,242,010	6,582,559
Deferred Inflows of Resources			
Deferred inflows from regulated activities	(5,375)	29,918	24,543
Net Position			
Net investment in capital assets	173,394	581,872	755,266
Restricted	220,065	87,143	307,208
Unrestricted	548,682	184,011	732,693
Total net position	$ 942,141	853,026	1,795,167
Commitments and contingencies			

See accompanying independent auditors' report.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Combining Statement of Revenues, Expenses, and Changes in Net Position

Year ended June 30, 2014

(Dollars in thousands)

	Sewer	Water	Combined total
Operating revenues:			
Customer services	$ 427,971	211,720	639,691
Other	3,797	4,529	8,326
Total operating revenues	431,768	216,249	648,017
Operating expenses:			
Operations	61,092	39,686	100,778
Maintenance	21,311	8,142	29,453
Payments in lieu of taxes	—	7,872	7,872
Engineering, general, and administrative	87,838	47,563	135,401
Total operating expenses	170,241	103,263	273,504
Income from operations before depreciation	261,527	112,986	374,513
Depreciation	138,092	54,970	193,062
Operating income	123,435	58,016	181,451
Regulatory accounting provisions:			
Change in reserves	204	(374)	(170)
Change in regulatory provisions, net	(5,138)	1,500	(3,638)
Total regulatory accounting provisions	(4,934)	1,126	(3,808)
Nonoperating income (expense):			
Operating grant	785	69	854
Investment income	3,032	2,401	5,433
Interest expense	(152,097)	(79,483)	(231,580)
Changes in derivative related accounts	2,528	412	2,940
Total nonoperating expense	(145,752)	(76,601)	(222,353)
Net loss before capital grants	(27,251)	(17,459)	(44,710)
Capital grants	4,446	1,512	5,958
Decrease in net position	(22,805)	(15,947)	(38,752)
Total net position – beginning of year	942,141	853,026	1,795,167
Total net position – end of year	$ 919,336	837,079	1,756,415

See accompanying independent auditors’ report.

MASSACHUSETTS WATER RESOURCES AUTHORITY

Combining Statement of Revenues, Expenses, and Changes in Net Position

Year ended June 30, 2013

(Dollars in thousands)

	Sewer	Water	Combined total
Operating revenues:			
Customer services	$ 413,841	203,574	617,415
Other	4,340	1,638	5,978
Total operating revenues	418,181	205,212	623,393
Operating expenses:			
Operations	62,413	39,012	101,425
Maintenance	20,125	6,831	26,956
Payments in lieu of taxes	—	7,640	7,640
Engineering, general, and administrative	85,987	45,342	131,329
Total operating expenses	168,525	98,825	267,350
Income from operations before depreciation	249,656	106,387	356,043
Depreciation	137,421	53,431	190,852
Operating income	112,235	52,956	165,191
Regulatory accounting provisions:			
Change in reserves	(922)	(476)	(1,398)
Change in regulatory provisions, net	14,456	10,859	25,315
Total regulatory accounting provisions	13,534	10,383	23,917
Nonoperating income (expense):			
Investment income	(1,605)	(1,474)	(3,079)
Interest expense	(156,404)	(80,133)	(236,537)
Changes in derivative related accounts	4,987	811	5,798
Total nonoperating expense	(153,022)	(80,796)	(233,818)
Net loss before capital grants	(27,253)	(17,457)	(44,710)
Capital grants	5,178	1,452	6,630
Decrease in net position	(22,075)	(16,005)	(38,080)
Total net position – beginning of year	964,216	869,031	1,833,247
Total net position – end of year	$ 942,141	853,026	1,795,167

See accompanying independent auditors' report.