

**Philadelphia Water Department  
Financial Statements  
Fiscal Year Ended June 30, 2014**

**CITY OF PHILADELPHIA WATER DEPARTMENT****2014 FINANCIAL STATEMENTS****TABLE OF CONTENTS**

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## **The City of Philadelphia Water Department Management Discussion and Analysis**

The Philadelphia Water Department is a municipal utility serving the citizens of the Philadelphia region by providing integrated water, wastewater, and stormwater services. The utility's primary mission is to plan for, operate, and maintain both the infrastructure and the organization necessary to purvey high-quality drinking water, to provide an adequate and reliable water supply for all household, commercial, and community needs, and to sustain and enhance the region's watersheds and quality of life by managing wastewater and stormwater effectively.

The Water Department was established by the City pursuant to the Charter with the power and duty to operate, maintain, repair, and improve the Water and Wastewater Systems. The Charter requires that the Water Rate Board must set rates and charges such as shall yield to the City at least an amount equal to operating expenses and debt service, on all obligation of the City in respect of the water, sewer, storm water systems and, in respect of water, sewer, and storm water revenue obligations of the City, such additional amounts as shall be required to comply with any rate covenant and sinking fund reserve requirements approved by ordinance of Council in connection with the authorization or issuance of water, sewer, and storm water revenue bonds, and proportionate charges for all services performed for the Water Department by all officers, departments, boards, or commissions of the City. The Charter also authorizes the Water Department, with the approval of City Council, to enter into contracts for supplying water service and sewer and sewage disposal service to users outside the limits of the City.

### **2014 Financial Highlights**

The Water Department met its bond coverage ratios for the year with a revenue bond coverage ratio of 1.22, a total debt service coverage ratio of 1.11, and a net operating revenue bond coverage ratio of 1.34 prior to the deduction of the transfer to the Rate Stabilization Fund.

At the end of the current fiscal year, the Water Fund's net position totaled \$970.5 million resulting from an excess of its assets over its liabilities; its unrestricted net position showed a balance of \$126.8 million.

The Water Fund's net position showed an increase of \$72.4 million during the current Fiscal Year compared with an increase of \$32.8 million for the prior fiscal year.

### **Overview of the Financial Statements**

This section serves as an introduction to the Basic Financial Statements. It represents management's examination and analysis of the Water Department's financial condition and performance. Summary financial data, key financial and operational indicators used in Water Department's budget, bond resolutions, and other management tools were used for the analysis.

The Financial Statements report information about the Water Department on the Full Accrual Accounting method as used by similar business activities in the private sector.

The Water Department's basic financial statements include the statement of net position, statement of revenues, expenses, and changes in net position, statement of cash flows, and notes to the financial statements.

The Water Department's financial statements are prepared in accordance with accounting principles promulgated by the Governmental Accounting Standards Board (GASB).

**Statement of Net Position:** The statement of net position presents the financial position of the Water Department. It presents information on the Water Department's assets, deferred outflows of resources, and liabilities with the difference between the three reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Water Department is improving or deteriorating.

**Statement of Revenues, Expenses, and Changes in Net Position:** The statement of revenues, expenses, and changes in net position presents information showing how the Water Department's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Revenues are recognized when earned, not when they are received. Expenses are recognized when incurred, not when they are paid. Thus, revenues and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g. salary and wages payable).

**Statement of Cash Flows:** The statement of cash flows presents information on the effects changes in assets, liabilities, and operations have on cash during the course of the fiscal year.

The Water Fund financial statements can be found following the Management Discussion and Analysis. The Notes provide additional information that is essential to a full understanding of the data provided in the Water Fund financial statements. In addition to the basic financial statements and accompanying notes, government accounting standards require presentation of required supplementary information ("RSI"). Following the RSI, the Water Department has presented other supplementary information ("OSI").

Please see the Comprehensive Annual Financial Report of the City of Philadelphia for complete financial information for the City and its component units, which can be found at <http://www.phila.gov/investor/CAFR.html>.

## Financial Analysis

### Net Position

A three year condensed summary of the Water Department's net position as of June 30 of each year is presented as follows:

Condensed Statement of Net Position  
(Thousands of Dollars)  
June 30

	2014	2013	2012 <sup>*</sup>
Assets:			
Current Assets	\$ 230,330	\$ 243,123	\$ 233,512
Capital Assets	2,070,492	2,019,350	1,938,001
Restricted Assets	690,596	526,249	631,960
Total Assets	2,991,418	2,788,722	2,803,473
Deferred Outflows of Resources	66,586	73,865	12,018
Total Assets and Deferred Outflows	3,058,004	2,862,587	2,815,491
Liabilities:			
Current Liabilities	214,671	211,872	200,381
Bonds Payable	1,809,952	1,702,895	1,698,122
Other Non-Current Liabilities	62,898	49,732	51,668
Total Liabilities	2,087,521	1,964,499	1,950,171
Net Position:			
Net Investment in Capital Assets	336,980	351,160	243,997
Restricted	506,669	472,310	439,084
Unrestricted	126,834	74,618	182,239
Total Net Position, as Restated	\$ 970,483	\$ 898,088	\$ 865,320

<sup>\*</sup>Fiscal Year 2012 was not restated for GASB Statement No. 65.

The Water Department's net position at June 30, 2014 was approximately \$970.5 million, a \$72.4 million or 8.1% increase from June 30, 2013. Total assets and deferred outflows of resources increased by \$195.4 million, or 6.8%, to \$3.1 billion, and total liabilities increased \$123.0 million, or 6.3%, to \$2.1 billion.

The following is a discussion of the more significant changes in assets and deferred outflows of resources, liabilities, and net position in fiscal year 2014:

- Capital assets, net of depreciation and amortization, increased by \$51.1 million to \$2.1 billion, or 2.5% as a result of capital additions of \$314.6 million, offset by depreciation of \$90.5 million and retirements of \$173.0 million.
- Current assets decreased by \$12.8 million to \$230.3 million, or 5.3%, due to decreases in cash, investments, and net accounts receivables.

- Restricted assets increased by \$164.3 million to \$690.6 million, or 31.2%, due to increases in the Water Capital Fund primarily due to the bond issuance in August 2013 and January 2014.
- Deferred outflows of resources decreased by \$7.3 million to \$66.6 million, or 9.9%, due to decreases in the fair market value of the Water Funds hedging instrument and amortization of the unamortized loss on refunded debt.
- Current liabilities increased by \$2.8 million to \$214.7 million, or 1.3%, primarily due to an increase in accrued expenses and other components offset by reductions in construction contracts payable.
- Bonds payable increased by \$107.1 million to \$1.8 billion, or 6.3%, primarily due to the bond issuances in August of 2013 and January of 2014 offset by the maturing principal of \$225.1 million during the year.
- Other non-current liabilities increased by \$13.2 million to \$62.9 million, or 26.5%, primarily due to an increase in the net pension obligation of \$17.7 million offset by decreases in the other non-current liabilities and derivative instrument liability.
- The Water Department's net position increased by \$72.4 million to \$970.5 million, or 8.1%, as a result of fiscal year 2014 operations and capital contributions.
- Net investment in capital assets decreased by \$14.2 million, or 4.0%, to \$337.0 million.
- Unrestricted net position increased by \$52.2 million, or 70.0%, to \$126.8 million. The unrestricted component of net position represents the net amount of total assets, deferred outflows of resources, and total liabilities that are not included in the determination of net investment in capital assets or restricted components of net position.

## Changes in Net Position

A condensed summary of the Water Department's Statement of Revenues, Expenses, and Changes in Net Position for the years ended June 30 is presented as follows:

### Condensed Statement of Revenues, Expenses, and Changes in Net Position (Thousands of Dollars) Year Ended June 30

	2014	2013	2012*
Operating Revenues:			
Charges for Goods and Services	\$ 630,429	\$ 600,156	\$ 591,571
Miscellaneous Operating Revenues	8,146	8,547	6,749
Operating Grants	1,399	2,285	3,481
Total Operating Revenues	639,974	610,988	601,801
Operating Expenses:			
Operating Expenses excluding Depreciation and Amortization	354,686	345,409	300,829
Depreciation and Amortization	90,523	89,045	92,113
Total Operating Expenses	445,209	434,454	392,942
Operating Income (Loss)	194,765	176,534	208,859
Nonoperating Revenues (Expenses):			
Federal, State, & Local Grants	-	880	479
Interest Income	4,207	12,079	3,334
Net Pension Obligation	(17,712)	2,839	(11,259)
Debt Service – Interest	(77,561)	(80,146)	(85,374)
Other Expenses	(2,971)	(1,665)	(1,243)
Total Nonoperating Revenues (Expenses)	(94,037)	(66,013)	(94,063)
Increase in Net Position before Transfers	100,728	110,521	114,796
Transfers Out	(28,333)	(21,380)	(27,460)
Change in Net Position	72,395	89,141	87,336
Net Position – Beginning of Period	898,088	808,947	777,984
Net Position – Ending of Period	\$ 970,483	\$ 898,088	\$ 865,320

\*Fiscal Year 2012 was not restated for GASB Statement No. 65.

Operating revenues increased by \$29.0 million to \$640.0 million due to increased revenue from a typical bill increase of 5.8% in fiscal year 2014.

Operating expenses increased by \$10.8 million to \$445.2 million due to increased costs for personnel services, purchase of services, materials and supplies, partially offset by lower expenses for employee benefits.

Non-operating expenses increased by \$28.0 million to \$94.0 million. The increase in non-operating expenses is due to the net pension obligation expense increase of \$20.6 million and the interest income decrease of \$7.9 million.

## Capital Assets and Debt Administration

### Capital Assets

The Water Department's investment in capital assets, net of accumulated depreciation, amounted to \$2.07 billion as of June 30, 2014. This represented an increase of \$51.1 million, or 2.5% over the previous year's total of \$2.02 billion. Capital assets consist primarily of land, infrastructure, construction in progress, buildings, and equipment. Infrastructure consists of water and wastewater transmission and distribution lines. The following is a summary of capital assets as of June 30:

Capital Asset Activity (Thousands of Dollars)			
	June 30		
	2014	2013	2012
Land	\$ 5,919	\$ 5,919	\$ 5,919
Construction in Progress	361,592	373,844	314,162
Infrastructure	2,269,015	2,167,639	2,087,956
Buildings and Equipment	1,623,520	1,591,073	1,572,818
Accumulated Depreciation	(2,189,554)	(2,119,125)	(2,042,854)
Total Capital Assets, net	<u>\$ 2,070,492</u>	<u>\$ 2,019,350</u>	<u>\$ 1,938,001</u>

### Long-Term Debt

As of June 30, 2014, the Water Department had \$1.87 billion of non-current liabilities outstanding. This was an increase of \$120.2 million or 6.9% from the previous year. The following is a summary of the non-current liability outstanding as of June 30:

Non-Current Liability Activity (Thousands of Dollars)			
	June 30		
	2014	2013	2012
Revenue Bonds – Net	\$ 1,809,952	\$ 1,702,895	\$ 1,698,122
Derivative Instrument	5,711	8,565	12,018
Other Non-Current Liabilities	30,514	32,205	27,849
Net Pension Obligation	26,673	8,962	11,801
Total Non-Current Liabilities	<u>\$ 1,872,850</u>	<u>\$ 1,752,627</u>	<u>\$ 1,749,790</u>

The following details activity to debt during 2014:

(Thousands of Dollars)	
Beginning balance at July 1, 2013	\$ 1,830,387
Debt issued	345,096
Less principal payments and amortization	(240,231)
Ending balance at June 30, 2014	<u>\$ 1,935,252</u>



More detailed information concerning long-term debt activity and capital asset activity is disclosed in Note 14 and Note 5, respectively, of the financial statements.

### **Budgetary Highlights**

Please see the supplementary Budgetary Comparison Schedule located in the Required Supplementary Information section.

### **Requests for Information**

This financial report is designed to provide a general overview of the City of Philadelphia Water Department's finances for all interested parties. Questions concerning any of the information provided in this report, or requests for additional information, should be addressed to the Philadelphia Water Department, Finance Division, Aramark Tower, 5th Floor, 1101 Market Street, Philadelphia, Pennsylvania 19107.

STATEMENTS OF NET POSITION  
JUNE 30, 2014 AND 2013

(Thousands of Dollars)

	June 30	
	2014	2013
<b>ASSETS:</b>		
<u>Current Assets:</u>		
Cash on Deposit and on Hand	\$ 30	\$ 30
Equity in Treasurer's Account	71,136	82,494
Due from Other Governments	176	76
Accounts Receivable	164,042	160,060
Allowance for Doubtful Accounts	(18,629)	(13,661)
Inventories	13,423	13,799
Receivables	152	325
Total Current Assets	230,330	243,123
<u>Noncurrent Assets:</u>		
Restricted Assets:		
Equity in Treasurer's Account	470,740	313,927
Sinking Funds and Reserves	219,013	210,990
Grants for Capital Purposes	-	252
Receivables	843	1,080
Total Restricted Assets	690,596	526,249
Capital Assets:		
Land	5,919	5,919
Infrastructure	2,269,015	2,167,639
Construction in Progress	361,592	373,844
Buildings and Equipment	1,623,520	1,591,073
Accumulated Depreciation	(2,189,554)	(2,119,125)
Total Capital Assets	2,070,492	2,019,350
Total Noncurrent Assets	2,761,088	2,545,599
<b>Total Assets</b>	<b>2,991,418</b>	<b>2,788,722</b>
<b>DEFERRED OUTFLOWS OF RESOURCES:</b>		
Deferred Outflow - Fin. Instruments	5,711	8,565
Unamortized Loss - Refunded Debt	60,875	65,300
<b>Total Deferred Outflows of Resources</b>	<b>66,586</b>	<b>73,865</b>
<b>LIABILITIES:</b>		
<u>Current Liabilities:</u>		
Vouchers Payable	8,230	6,763
Accounts Payable	11,664	12,655
Salaries & Wages Payable	4,819	4,187
Construction Contracts Payable	22,783	27,530
Accrued Expenses	27,477	23,812
Due to Other Components	3,607	-
Unearned Revenue	8,923	7,531
Funds Held in Escrow	1,868	1,902
Current Portion of Long Term Obligations	125,300	127,492
Total Current Liabilities	214,671	211,872
<u>Noncurrent Liabilities:</u>		
Bond Payable - Net	1,809,952	1,702,895
Derivative Instrument Liability	5,711	8,565
Other Noncurrent Liabilities	30,514	32,205
Net Pension Liability	26,673	8,962
Total Noncurrent Liabilities	1,872,850	1,752,627
<b>Total Liabilities</b>	<b>2,087,521</b>	<b>1,964,499</b>
<b>NET POSITION:</b>		
Net Investment in Capital Assets	336,980	351,160
Restricted For:		
Capital Projects	102,860	99,856
Debt Service	219,013	210,990
Rate Stabilization	184,796	161,464
Unrestricted	126,834	74,618
<b>Total Net Position</b>	<b>\$ 970,483</b>	<b>\$ 898,088</b>

**STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION  
FOR FISCAL YEAR ENDED JUNE 30, 2014 AND 2013**

(Thousands of Dollars)

	<b>Year Ended June 30</b>	
	<b>2014</b>	<b>2013</b>
<u>Operating Revenues:</u>		
Charges for Goods and Services	\$ 630,429	\$ 600,156
Miscellaneous Operating Revenues	8,146	8,547
Operating Grants	1,399	2,285
Total Operating Revenues	639,974	610,988
<u>Operating Expenses:</u>		
Personal Services	112,820	110,784
Purchase of Services	90,611	88,395
Materials and Supplies	43,453	38,409
Employee Benefits	102,623	104,713
Indemnities and Taxes	5,179	3,108
Depreciation and Amortization	90,523	89,045
Total Operating Expenses	445,209	434,454
Operating Income	194,765	176,534
<u>Nonoperating Expenses:</u>		
Federal, State, & Local Grants	-	880
Interest Income	4,207	12,079
Net Pension Obligation	(17,712)	2,839
Debt Service - Interest	(77,561)	(80,146)
Other Expenses	(2,971)	(1,665)
Total Nonoperating Expenses	(94,037)	(66,013)
Increase in Net Position before Transfers	100,728	110,521
Transfers Out	(28,333)	(21,380)
Change in Net Assets	72,395	89,141
Net Position - Beginning of Year	898,088	865,320
Adjustment (Note 23)	-	(56,373)
<b>Net Position - End of Year</b>	<b>\$ 970,483</b>	<b>\$ 898,088</b>

**STATEMENTS OF CASH FLOWS  
FOR FISCAL YEAR ENDED JUNE 30, 2014 AND 2013**

(Thousands of Dollars)

	<b>Year Ended June 30</b>	
	<b>2014</b>	<b>2013</b>
<b><u>Cash Flows from Operating Activities:</u></b>		
Receipts from Customers	\$ 640,819	\$ 602,342
Payments to Suppliers	(130,852)	(129,513)
Payments to Employees	(216,574)	(208,891)
Claims Paid	(5,179)	(5,090)
<b>Net Cash Provided by Operating Activities</b>	<b>288,214</b>	<b>258,848</b>
<b><u>Cash Flows from Non-Capital Financing Activities:</u></b>		
Operating Grants Received	1,649	2,285
Operating Subsidies and Transfers to Other Funds	(31,322)	(21,380)
<b>Net Cash Used by Non-Capital Financing Activities</b>	<b>(29,673)</b>	<b>(19,095)</b>
<b><u>Cash Flows from Capital &amp; Related Financing Activities:</u></b>		
Proceeds from Capital Debt	229,204	97,860
Capital Contributions Received	-	628
Acquisition and Construction of Capital Assets	(142,039)	(153,388)
Interest Paid on Capital Debt	(74,701)	(76,180)
Principal Paid on Capital Debt	(127,009)	(207,220)
<b>Net Cash Used by Non-Capital Financing Activities</b>	<b>(114,545)</b>	<b>(338,300)</b>
<b><u>Cash Flows from Investing Activities:</u></b>		
Interest and Dividends	1,459	(63,653)
<b>Net Cash Provided by (Used in) Investing Activities</b>	<b>1,459</b>	<b>(63,653)</b>
<b>Net Increase (Decrease) in Cash &amp; Cash Equivalents</b>	<b>145,455</b>	<b>(162,200)</b>
Balances - Beginning of the Year	396,451	558,651
<b>Balances - End of the Year</b>	<b>\$ 541,906</b>	<b>\$ 396,451</b>
<b><u>Reconciliation of Operating Income to</u></b>		
<b><u>Net Cash Provided by Operating Activities:</u></b>		
Operating Income	194,765	176,534
Adjustments to Reconcile Operating Income to Net Cash		
Provided (Used) by Operating Activities:		
Depreciation Expense	90,523	89,045
Change in Assets and Liabilities:		
Receivables, Net	(547)	(9,551)
Inventories	376	(343)
Accounts and Other Payables	3,396	(4,134)
Accrued Expenses	(1,691)	6,392
Unearned Revenue	1,392	905
<b>Net Cash Provided by Operating Activities</b>	<b>\$ 288,214</b>	<b>\$ 258,848</b>
<b><u>Reconciliation of Cash and Cash Equivalents to Statement of Net Position</u></b>		
Cash on Deposit and on Hand	30	30
Equity in Treasurer's Account - Current Portion	71,136	82,494
Equity in Treasurer's Account - Noncurrent Portion	470,740	313,927
<b>Total Cash and Cash Equivalents</b>	<b>\$ 541,906</b>	<b>\$ 396,451</b>

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

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 1:      REPORTING ENTITY**

The City of Philadelphia was founded in 1682 and was merged with the county in 1854. The City of Philadelphia, Pennsylvania (the “City” or “Philadelphia”), was incorporated in 1789 by an Act of the General Assembly of the Commonwealth of Pennsylvania (the “Commonwealth”) (predecessors of the City under charters granted by William Penn in his capacity as proprietor of the colony of Pennsylvania may date to as early as 1684). In 1854, the General Assembly of the Commonwealth, by an act commonly referred to as the Consolidation Act, made the City’s boundaries coterminous with the boundaries of Philadelphia County (the same boundaries that exist today) (the “County”), abolished all governments within these boundaries other than the City and the County and consolidated the legislative functions of the City and the County. Article 9, Section 13 of the Pennsylvania Constitution abolished all county offices in the City and provides that the City performs all functions of county government and that laws applicable to counties apply to the City.

Since 1952, the City has been governed under a Home Rule Charter authorized by the General Assembly of the Commonwealth (First Class City Home Rule Act, Act of April 21, 1949, P.L. 665, Section 17) and adopted by the voters of the City. The Home Rule Charter, as amended and supplemented to this date, provides, among other things, for the election, organization, powers and duties of the legislative branch (the “City Council”); the election, organization, powers and duties of the executive and administrative branch; and the basic rules governing the City’s fiscal and budgetary matters, contracts, procurement, property and records. The Home Rule Charter, as amended, also provides for the governance of the School District of Philadelphia (the “School District”) as a home rule school district. Certain other constitutional provisions and Commonwealth statutes continue to govern various aspects of the City’s affairs, notwithstanding the broad grant of powers of local self-government in relation to municipal functions set forth in the First Class City Home Rule Act.

The City's Water Department supplies water and provides wastewater treatment services to residents of Philadelphia and portions of Bucks, Montgomery, and Delaware Counties, although over 90% of those served are residents of the City.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 1:      REPORTING ENTITY (CONTINUED)**

There are two principal governmental entities in Philadelphia: (1) the City of Philadelphia, which performs both the ordinary Municipal functions and the traditional County functions; and the School District of Philadelphia, which is part of the Public Education System of the Commonwealth of Pennsylvania. In addition to the School District of Philadelphia, there are a number of other governmental and quasi-governmental entities operating within the City. The financial statements as set forth herein present only the operations of the City of Philadelphia Water Department (“Water Department”) that is a Department of the City and is included in the financial statements of the City.

The Philadelphia Water Department serves the Greater Philadelphia region by providing an integrated water, wastewater, and stormwater system. The utility's primary mission is to plan for, operate and maintain both the infrastructure and the organization necessary to purvey high quality drinking water, to provide an adequate and reliable water supply for all household, commercial, and community needs, and to sustain and enhance the region's watersheds and quality of life by managing wastewater and stormwater effectively. In fulfilling its mission, the utility seeks to be customer-focused, delivering services in a fair, equitable, and cost-effective manner, with a commitment to public involvement. Having already served the City and region for nearly two centuries, the utility's commitment for the future includes an active role in the economic development of Greater Philadelphia and a legacy of environmental stewardship.

In order to accomplish its mission and pursuant to the Philadelphia Home Rule Charter, the Water Department has the power and duty to operate, maintain, repair and improve the City's water and wastewater systems. The Water Department is managed by a Commissioner who is appointed by the City's Managing Director with the approval of the Mayor.

The operations of the activity of the Water Department are accounted for with a separate set of balancing accounts that comprise its assets, liabilities, and net position, revenues and expenses. The activity of the Water Department is grouped in the financial statements into the broad category referred to as an enterprise fund. Such activities are used to account for operations (1) that are financed and operated in a manner similar to private business enterprises – where the intent of the Government Body is that costs (expenses, including depreciation) of providing goods and services to the general public on a continuous basis be recovered primarily through user charges or (2) where the Government Body has decided that periodic determination of revenues earned, expenses occurred, and/or net income is appropriate for capital maintenance, public policy, management's control of accountability, and other purposes.

The activities of the Water Department are segregated as follows:

- The Operating Fund is used to account for the operations of the water and waste water systems.
- The Revenue Bond Sinking Fund is used to account for the payment of interest of the outstanding debt.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 1: REPORTING ENTITY (CONTINUED)**

- The Debt Reserve Fund shall be funded from the proceeds of each series of Water and Wastewater Revenue Bonds; provided, however, that if the Supplemental Ordinance authorizing a series of Water and Wastewater Revenue Bonds shall so authorize, the deposit to the Debt Reserve Account in respect of such Water and Wastewater Revenue Bonds may be accumulated from project revenues over a period of not more than three fiscal years after the issuance and delivery of such Water and Wastewater Revenue Bonds. The moneys and investments in the Debt Reserve Account shall be held and maintained in an amount equal at all times to the Debt Reserve Requirement. If at any time the moneys in the Debt Service Account of the Sinking Fund shall be insufficient to pay as and when due the principal of (and premium, if any) or interest on any Water and Wastewater Revenue Bonds or other obligations payable from the Debt Service Account (including obligations arising in connection with Qualified Swap Agreements and Credit Facilities), the fiscal agent is required to pay over from the Debt Reserve Account the amount of such deficiency for deposit in the Debt Service Account. With respect to any issue of Water and Wastewater Revenue Bonds, in lieu of the required deposit into the Debt Reserve Account, the City may cause to be deposited into the Debt Reserve Account a surety bond, an insurance policy or an irrevocable letter of credit meeting the requirements of the General Ordinance and the Bond Committee Determination relating to such issue.

The Debt Reserve Account Amendment authorizes (i) the Director of Finance to apply moneys currently on deposit in the Debt Reserve Account to purchase a surety bond or insurance policy complying with the terms of the General Ordinance (described below), (ii) the transfer of the resulting excess moneys in the Debt Reserve Fund to the Revenue Fund and from there, upon compliance with the provisions of the General Ordinance to a new account in the Residual Fund called the Special Water Infrastructure Account and (iii) the application of the moneys deposited in the Special Water Infrastructure Account to the cost of renewals, replacements and improvements to the water and wastewater systems.

- The Rate Stabilization Fund was created with the sale of the Series 1993 Revenue Bonds on August 20, 1993. The purpose of the Fund is to maintain assets to be drawn down to offset future deficits (and corresponding rate increase requirements) in the Water Department Operating Fund.

During Fiscal 2014 the fund had the following activity:

Balance at July 1, 2013	\$161,463,768
Deposit from Operating Fund	22,924,772
Interest Earnings	407,041
Deposit to Operating Fund	-
Balance at June 30, 2014	<u>\$184,795,581</u>

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 1: REPORTING ENTITY (CONTINUED)**

During Fiscal 2013 the fund had the following activity:

Balance at July 1, 2012	\$165,906,600
Deposit from Operating Fund	-
Interest Earnings	223,120
Deposit to Operating Fund	(4,665,952)
Balance at June 30, 2013	<u>\$161,463,768</u>

- The Residual Fund was created with the sale of the Series 1993 Revenue Bonds on August 20, 1993. The purpose of the Fund is to maintain the remaining assets after payment of all operating expenses, payment of all debt service obligations including payments under a swap agreement, scheduled transfers to the Rate Stabilization Fund, and required deposits to the Capital Account of the Construction Fund.

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The accompanying financial statements include all funds which are controlled by the Philadelphia Water Department. The financial statements have been prepared in accordance with Generally Accepted Accounting Principles as they apply to governmental units. The Governmental Accounting Standards Board (GASB) of the American Institute of Certified Public Accountants is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies.

**A. Basis of Accounting**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and deferred outflows of resources, liabilities, and net position and disclosures at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of timing of related cash flows. Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.



**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
(CONTINUED)**

**A. Basis of Accounting (Continued)**

Operating revenues and expenses are distinguished from non-operating items in the statement of revenues, expenses and changes in net position. Operating revenues and expenses result from providing services in connection with the Water Department's principle ongoing operations. Principal operating revenues of the Water Department are charges to customers for water use and watershed collection, transmission and treatment. When calculating user fees charged to customers, the Water Department includes a component for the repayment of principal on the Water Department's outstanding debt. Operating expenses include the cost of providing water and watershed services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. The principal non-operating revenues of the Water Department are interest and grants. The principal non-operating expenses of the Water Department include interest expense and pension expense.

**B. Capital Assets**

Capital assets are defined by the City as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of three years. The expenses are reported at cost including any liability for contract retainage and construction costs payable.

Contributed assets are carried at estimated market value at the time of contribution. Depreciation is determined using the straight-line method over their estimated useful lives as follows:

Computer equipment	3 years
Automotive	5 years
Leasehold Improvements	8 years
General and monitoring equipment	10-20 years
Buildings	40 years
Reconstructed transmission and distribution lines	40 years
New transmission and distribution lines	50 years

Normal maintenance and repairs are charged to operations as incurred. Renewals and betterments are capitalized and depreciated based upon the expected life of such improvements.

Cost of construction includes all direct contract costs plus overhead charges. Overhead costs include direct and indirect engineering costs and interest incurred during the construction period on projects financed with revenue bond proceeds. Interest is capitalized by applying the average financing rate during the year to construction costs incurred. Interest earnings on bond proceeds reduce the amount capitalized. Capitalization of interest during construction for fiscal year 2014 was \$3,926,863 and for fiscal year 2013 was \$12,951,027.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
(CONTINUED)**

**C. Bond Discount**

Bond discounts are deferred and amortized by the bonds outstanding method, which appropriates the interest method. For financial reporting purposes, bond discounts and premiums are offset against bonds payable.

**D. Inventories**

The materials and supplies inventory is priced using the “moving average cost” method.

**E. Deferred Refunding Loss**

The accounting loss incurred by the Water Department related to the refunding of certain bonds is deferred and amortized over the life of the original bond or the refunded bonds whichever is shorter.

**F. Accounts Receivables**

Accounts receivable consist of billed retail and wholesale water and sewer charges that have not been collected as of June 30. The Water Department evaluates the collection of individual account balances and if necessary, records an allowance for doubtful accounts. The Water Department’s policy is to file a lien against the respective property for delinquent water, sewer, and storm water customers. The Water Department’s policy regarding its water customers is to discontinue services for those that refuse to pay, but only as a last resort. As of June 30, 2014 and 2013 the allowance for doubtful accounts was \$18,629,063 and \$13,660,860 respectively.

**G. Unbilled Revenue**

The Water Department bills residential water and sewer customers on a monthly basis and wholesale water and sewer customers on a monthly basis. Revenue earned for services provided through June 30 but unbilled is included in accounts receivable on the accompanying financial statements.

**H. Insurance**

The City, except for the Airport and certain other properties, is self-insured for most fire and casualty losses to its structures and equipment and provides statutory workers’ compensation, unemployment benefits, and health and welfare to its employees through a self-insured plan. Construction contractors are required to carry protective general liability insurance indemnifying the City and the Contractor.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
(CONTINUED)**

**I. Cash and Investments**

The Water Department's cash and investments are held in segregated operating and capital accounts. Sinking funds and reserves are maintained in segregated investment accounts to comply with reserve and other requirements of the bond covenants.

All highly liquid investments (except for Repurchase Agreements) with a maturity of three months or less when purchased are considered to be cash equivalents.

The investments of the City are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on national or international exchanges are valued at the last reported sales price. The fair value of real estate investments is based on independent appraisals. Investments, which do not have an established market, are reported at estimated fair value.

Statutes authorize the City to invest in obligations of the Treasury, agencies, and instruments of the United States, repurchase agreements, collateralized certificates of deposit, bank acceptance or mortgage obligations, certain corporate bonds, and money market funds.

**J. Restricted Assets**

Restricted assets represent revenues set-aside for liquidation of specific obligations, as detailed in Note 8.

**K. Unearned Revenues**

Unearned revenues represent funds received in advance of being earned. In the Water Department, unearned revenues relate principally to over paid water and sewer bills.

**L. Payment to City**

In accordance with an agreement between the Finance Director and the Water Department, the Finance Director may transfer to the General Fund up to a limit of \$4,994,000 in any fiscal year in "excess interest earnings" as defined by the Rate Covenants under the Ordinance. In fiscal year 2014 and 2013, excess interest earnings of \$400,364 and \$560,156, respectively, were transferred to the General Fund of the City.

**M. Transfers for Long Term Contracts**

In addition to the transfer of funds to the General Fund of the City, the Water Department had operating transfers of \$27,932,268 and \$20,819,479 in fiscal year 2014 and 2013, respectively, to the Philadelphia Municipal Authority ("PMA") for the long-term contracts described in Note 19 A, B, and C.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
(CONTINUED)**

**N. Net Position**

The basic financial statements utilize the net position presentation, net position is categorized as net investment in capital assets, restricted, and unrestricted.

- *Net Investment in Capital Assets* – This category is intended to reflect the portion of net position that is allocated with non-liquid capital assets, less outstanding capital asset related debt.
- *Restricted Net Position* – This category represents external restrictions imposed by creditors, grantors, contributors, laws and regulations of other governments, and restrictions imposed by law through constitutional provisions or enabling legislation.
- *Unrestricted Net Position* – This category represents net position of the Water Department, not restricted for any project or other purpose.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

**O. Deferred Outflows / Inflows of Resources**

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to future period(s) and so will not be recognized as an outflow of resources (expense) until then. The Water Department has two items that qualify for reporting in this category. The statement of net position reports a deferred loss on refunded debt and the change in fair value of a hedging derivative instrument.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Water Department does not have an item that qualified for reporting in this category.

**P. Accounting Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results may differ from those estimates.

**Q. Reclassifications**

For comparative purposes, certain prior year financial statement amounts have been reclassified to conform to current year presentation. The reclassification had no effect on net position.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 2: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES  
(CONTINUED)**

**R. Adoption of Governmental Accounting Standards Board Statements**

The Water Department adopted the requirements of GASB Statement No. 66, *“Technical Corrections – 2012 – an amendment of GASB Statements No. and No. 62.”* The adoption of this statement had no effect on previously reported amounts.

The Water Department adopted the requirements of GASB Statement No. 67 *“Financial Reporting for Pension Plans – an amendment of GASB Statement No. 25”*. The adoption of this statement has no effect on the previously reported amounts.

The Water Department adopted the requirements of GASB Statement No. 70, *“Accounting and Financial Reporting for Nonexchange Financial Guarantees”*. The adoption of this statement had no effect on previously reported amounts.

**S. Pending Changes in Accounting Principles**

In June 2012, the GASB issued a Statement No. 68, *“Accounting and Financial Reporting for Pensions– an amendment of GASB Statement No. 27”*. The Water Department is required to adopt statement No. 68 for its fiscal year 2015 financial statements.

In January 2013, the GASB issued a Statement No. 69, *“Government Combinations and Disposals of Government Operations”*. The Water Department is required to adopt statement No. 69 for its fiscal year 2015 financial statements.

In November 2013, the GASB issued a Statement No. 71, *“Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68”*. The Water Department is required to adopt statement No. 71 for its fiscal year 2015 financial statements.

The Water Department has not yet completed the various analyses required to estimate the financial statement impact of these new pronouncements.

**NOTE 3: DEPOSITS AND INVESTMENTS**

**A. Deposits**

State statutes require banks to collateralize City deposits at amounts equal to or in excess of the City’s balance. Such collateral is to be held by the Federal Reserve Bank or the trust department of a commercial bank other than the pledging bank. At June 30, 2014 and June 30, 2013, all of the collateralized securities were held in the City’s name except for \$106 million and \$121 million, respectively, which was collateralized but held in the pledging institution’s name.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 3: DEPOSITS AND INVESTMENTS (CONTINUED)**

**B. Investments**

The City has established a comprehensive investment policy. To minimize custodial credit risk for investments, the City's policy is to select custodian banks that are members of the Federal Reserve System to hold its investments. Delivery of the applicable investment documents to the City's custodian is required for all investments.

As of June 30, 2014 the fair values of the Water Department's investments consist of the following:

(Thousands of Dollars)		
Classifications	Fair Value	Percent of Total
U.S. Government Securities	\$ 370,176	74.91%
U.S. Government Agency Securities	98,400	19.91%
Corporate Bonds	11,313	2.29%
Other Bonds and Investments	14,300	2.89%
<b>Grand Total</b>	<b>\$ 494,189</b>	<b>100.00%</b>

As of June 30, 2013, the fair values of the Water Department's investments consist of the following:

(Thousands of Dollars)		
Classifications	Fair Value	Percent of Total
U.S. Government Securities	\$ 336,277	80.84%
U.S. Government Agency Securities	43,542	10.46%
Corporate Bonds	30,025	7.22%
Other Bonds and Investments	6,149	1.48%
<b>Grand Total</b>	<b>\$ 415,993</b>	<b>100.00%</b>

*Interest Rate Risk:* The City's investment portfolio is managed to accomplish preservation of principal, maintenance of liquidity, and to maximize the return on investments. To limit its exposure to fair value losses from rising interest rates, the City's investment policy limits investments to maturities of no longer than 2 years.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 3: DEPOSITS AND INVESTMENTS (CONTINUED)**

**B. Investments (Continued)**

As of June 30, 2014 the maturities of the Water Department's investments were as follows:

	(Thousands of Dollars)	
	<b>Less Than 1</b>	
<b>Classifications</b>	<b>Year</b>	<b>1 - 2 Years</b>
U.S. Government Securities	\$ 260,368	\$ 109,808
U.S. Government Agency Securities	49,071	49,329
Corporate Bonds	11,313	-
Other Bonds and Investments	6,266	8,034
<b>Grand Total</b>	<b>\$ 327,018</b>	<b>\$ 167,171</b>

As of June 30, 2013 the maturities of the Water Department's investments were as follows:

	(Thousands of Dollars)	
	<b>Less Than 1</b>	
<b>Classifications</b>	<b>Year</b>	<b>1 - 2 Years</b>
U.S. Government Securities	\$ 187,315	\$ 148,962
U.S. Government Agency Securities	5,953	37,589
Corporate Bonds	26,089	3,936
Other Bonds and Investments	6,149	-
<b>Grand Total</b>	<b>\$ 225,506</b>	<b>\$ 190,487</b>

*Credit Risk:* The City's policy to limit credit risks is to invest in US Government securities (12.86%) or US Government Agency obligations (4.80%). The US Government Agency obligations must be rated AAA by Standard & Poor's Corp. ("S&P") or Aaa by Moody's Investor Services ("Moody's"). All US Government Securities meet the criteria. The City's investment in Commercial Paper (4.21%) must be rated A1 by S&P and/or M1G1 by Moody's and the senior long-term debt of the issuer must not be rated lower than A by S&P and/or Moody's. Commercial Paper is also limited to 25% of the portfolio. All commercial paper investments meet the criteria. Of the corporate bonds held by the City, 9.94% had a S&P rating of AAA to AA. Cash accounts are swept nightly and idle cash invested in money market funds (short term investment pools). Short Term Investment Pools are rated AAA by S&P and Aaa by Moody's. The Short Term Investment Pools' fair value is the same as the value of the pool shares. The City limits its foreign currency risk by investing in certificates of deposits and banker's acceptances issued or endorsed by non-domestic banks that are denominated in US dollars, providing that the banking institution has assets of not less than \$100 million and has a Thompson's Bank Watch Service "Peer Group Rating" not lower than II. At the end of the fiscal year, the City did not have any investments of that nature.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 4: ACCOUNTS RECEIVABLE**

Balances of accounts receivable and allowance for doubtful accounts consisted of the following:

**FISCAL YEAR ENDED JUNE 30, 2014**

**Accounts Receivable:**

Billed in the Last Twelve Months	\$ 138,553,005
Billed in 15-year Cycle Billing	-
Penalties on Receivables	13,992,499
Other Receivables	<u>11,496,268</u>
<b>Total</b>	<u><u>\$ 164,041,772</u></u>
Bad Debts Written Off	<u><u>\$ 36,402,784</u></u>
Allowance for Doubtful Accounts	<u><u>\$ 18,629,063</u></u>

**FISCAL YEAR ENDED JUNE 30, 2013**

**Accounts Receivable:**

Billed in the Last Twelve Months	\$ 112,392,541
Billed in 15-year Cycle Billing	-
Penalties on Receivables	33,165,628
Other Receivables	<u>14,502,308</u>
<b>Total</b>	<u><u>\$ 160,060,477</u></u>
Bad Debts Written Off**	<u><u>\$ 125,750,066</u></u>

**Allowance for Doubtful Accounts:**

Billed in the Last Twelve Months	\$ 2,470,849
Billed in 15-year Cycle Billing	6,436,465
Penalties on Receivables	4,753,546
Other Receivables	<u>-</u>
<b>Total</b>	<u><u>\$ 13,660,860</u></u>

\*\*During FY 2013, a proposal was presented and accepted by the City's Accounts Review Panel to write off aged receivables over one year old.



**PHILADELPHIA WATER DEPARTMENT**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**JUNE 30, 2014**

**NOTE 5: PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment at June 30, 2014 and 2013 consisted of the following:

	Beginning Balance	Additions	Dispositions	Ending Balance
<b>Fiscal Year Ended June 30, 2014</b>				
<u>Capital Assets Not Being Depreciated</u>				
Land	\$ 5,919,160	\$ -	\$ -	\$ 5,919,160
Construction in Progress	373,844,154	140,968,008	(153,220,212)	361,591,950
Total Capital Assets Not Being Depreciated	<u>\$ 379,763,314</u>	<u>\$ 140,968,008</u>	<u>\$ (153,220,212)</u>	<u>\$ 367,511,110</u>
<u>Capital Assets Being Depreciated</u>				
Buildings and related improvements	1,517,587,479	44,662,033	(10,269,725)	1,551,979,787
Intangible Assets	12,234,866	738,640	-	12,973,506
Equipment	73,485,553	20,255,147	(22,200,434)	71,540,266
Infrastructure	2,155,403,733	107,998,169	(7,360,430)	2,256,041,472
Total Capital Assets Being Depreciated	<u>\$ 3,758,711,631</u>	<u>\$ 173,653,989</u>	<u>\$ (39,830,589)</u>	<u>\$ 3,892,535,031</u>
<u>Less Accumulated Depreciation For:</u>				
Buildings and related improvements	(888,398,708)	(41,711,939)	7,267,028	(922,843,619)
Intangible Assets	(6,129,171)	(1,260,419)	-	(7,389,590)
Equipment	(65,974,792)	(2,723,579)	5,466,741	(63,231,630)
Infrastructure	(1,158,622,726)	(44,826,982)	7,360,430	(1,196,089,278)
Total Accumulated Depreciation	<u>(2,119,125,397)</u>	<u>(90,522,919)</u>	<u>20,094,199</u>	<u>(2,189,554,117)</u>
Total Capital Assets, Being Depreciated, Net	<u>1,639,586,234</u>	<u>83,131,070</u>	<u>(19,736,390)</u>	<u>1,702,980,914</u>
Total Capital Assets	<u>\$ 2,019,349,548</u>	<u>\$ 224,099,078</u>	<u>\$ (172,956,602)</u>	<u>\$ 2,070,492,024</u>
<b>Fiscal Year Ended June 30, 2013</b>				
<u>Capital Assets Not Being Depreciated</u>				
Land	\$ 5,919,160	\$ -	\$ -	\$ 5,919,160
Construction in Progress	314,162,257	63,795,220	(4,113,323)	373,844,154
Total Capital Assets Not Being Depreciated	<u>\$ 320,081,417</u>	<u>\$ 63,795,220</u>	<u>\$ (4,113,323)</u>	<u>\$ 379,763,314</u>
<u>Capital Assets Being Depreciated</u>				
Buildings and related improvements	1,502,631,913	19,703,244	(4,747,678)	1,517,587,479
Intangible Assets	11,414,581	820,285	-	12,234,866
Equipment	70,186,353	20,219,282	(16,920,082)	73,485,553
Infrastructure	2,076,541,650	86,819,904	(7,957,821)	2,155,403,733
Total Capital Assets Being Depreciated	<u>\$ 3,660,774,497</u>	<u>\$ 127,562,715</u>	<u>\$ (29,625,581)</u>	<u>\$ 3,758,711,631</u>
<u>Less Accumulated Depreciation For:</u>				
Buildings and related improvements	(852,672,838)	(40,473,548)	4,747,678	(888,398,708)
Intangible Assets	(4,946,699)	(1,182,472)	-	(6,129,171)
Equipment	(64,047,323)	(2,670,465)	742,996	(65,974,792)
Infrastructure	(1,121,187,009)	(44,718,881)	7,283,164	(1,158,622,726)
Total Accumulated Depreciation	<u>(2,042,853,869)</u>	<u>(89,045,366)</u>	<u>12,773,838</u>	<u>(2,119,125,397)</u>
Total Capital Assets, Being Depreciated, Net	<u>1,617,920,628</u>	<u>38,517,349</u>	<u>(16,851,743)</u>	<u>1,639,586,234</u>
Total Capital Assets	<u>\$ 1,938,002,045</u>	<u>\$ 102,312,569</u>	<u>\$ (20,965,066)</u>	<u>\$ 2,019,349,548</u>

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 6: LEASES**

The Water Department enters into various operating leases to finance the purchase of photocopier and computer equipment. Leases are defined by the Financial Accounting Standard Board in Statement 13, Accounting for Leases. Lease payments consisted of \$1,848,062 in fiscal year 2014, and \$1,514,466 in fiscal year 2013. The assets acquired through the leases are shown as equipment within the Capital Asset Note (See Note 5).

**NOTE 7: IMPAIRED ASSETS**

Government Accounting Standards Board (GASB) Statement 42 requires the disclosure of the impairment of any major capital assets. Over the years, there have been a number of the Water Department's assets that were either damaged or destroyed, were abandoned or became functionally obsolete.

One facility remains in service, which has become "functionally obsolescent", the portion of our Biosolids Recycling Center which performs composting. Composting of our sludge products was stopped in approximately March of 2007 as an interim solution to the air management problems that have occurred at this site. A permanent solution for sludge processing that does not involve composting is being utilized by the Water Department through the biosolids treatment and utilization plant operated by Philadelphia Biosolids Services, LLC (see Note 19). The Water Department's engineering division estimates the value of the compost facilities that are "functionally obsolescent" (which were built in conjunction with the remaining BRC facilities which will remain in service such as the mixing/receiving building, administrative offices and the dewatering facility) to be in the area of \$20 million, including the value of any land acquisition and site preparation costs.

No asset impairments occurred during fiscal year 2014 and 2013.

**NOTE 8: RESTRICTED ASSETS**

Assets whose use is limited to a specific purpose have been classified as "restricted" in the Statement of Fund Net Position. Restricted assets as of June 30, 2014, are comprised of the following:

	(Thousands of Dollars)	
	<b>Cash and</b>	<b>Accrued</b>
	<b>Investments</b>	<b>Interest</b>
Amounts Reserved for:		
Capital Projects	\$ 260,834	\$ 505
Rate Stabilization	184,631	165
Residual	25,275	-
Debt Service	219,013	173
<b>Total</b>	<b>\$ 689,753</b>	<b>\$ 843</b>

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 8: RESTRICTED ASSETS (CONTINUED)**

Restricted assets as of June 30, 2013, are comprised of the following:

	(Thousands of Dollars)		
	<b>Cash and</b>	<b>Accrued</b>	<b>Grants</b>
	<b>Investments</b>	<b>Interest</b>	<b>Receivable</b>
Amounts Reserved for:			
Capital Projects	\$ 150,603	\$ 286	\$ 252
Rate Stabilization	161,239	225	-
Residual	2,085	2	-
Debt Service	210,990	567	-
<b>Total</b>	<b>\$ 524,917</b>	<b>\$ 1,080</b>	<b>\$ 252</b>

**NOTE 9: VACATION LEAVE**

Employees are credited with vacation at rates which vary according to length of service. Vacation may be taken or accumulated up to certain limits until paid upon retirement or termination. Employees' vacation time accrued under Other Noncurrent Liabilities on the Statement of Net Position in Fiscal Year 2014 was \$10,170,963 and in Fiscal Year 2013 was \$9,972,902. The expense for vacation pay is recognized in the year earned.

**NOTE 10: SICK LEAVE**

Employees are credited with varying amounts of sick leave per year according to type of employee and/or length of service. Employees may accumulate unused sick leave to 200 days and union represented employees may convert up to 20 sick days per year to vacation days at a ratio of 2 for 1. Non-uniformed employees (upon retirement only) are paid 30% of unused sick time, not to exceed predetermined amounts. Employees, who separate for any reason other than indicated above, forfeit their entire sick leave. The City budgets for and charges the cost of sick leave as it is taken.

**NOTE 11: ACCOUNTING FOR THE NEW RIVER CITY PROJECT FUNDS –  
WATER SINKING FUND RESERVE SUBSTITUTION**

Pursuant to the Water Department's General Bond Ordinance, the Sinking Fund Reserve provides a reserve against default of the payment of principal and interest on Water Revenue Bonds when due.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 11: ACCOUNTING FOR THE NEW RIVER CITY PROJECT FUNDS –  
WATER SINKING FUND RESERVE SUBSTITUTION (CONTINUED)**

The New River City Ordinance dated January 23, 2007 (Bill No 060005) authorized the purchase and deposit of a surety bond that meets the requirements of the General Ordinance to replace \$67,000,000 of the Sinking Fund reserve Balance. The \$67,000,000 will be used as follows:

Cost of the surety bond	\$2,010,000
Legal and financial services	290,000
Management fees	375,000
Costs of certain water and sewer infrastructure components of the New River City Program	64,325,000
Total	<hr/> \$67,000,000 <hr/>

The prepaid surety bond was recorded as an asset in the Sinking Fund Reserve and amortized over the lives of the outstanding bonds.

In connection with the New River City Program, the Water Department executed a program agreement with Philadelphia Authority for Industrial Development (“PAID”) to provide program management and oversight for the program. To date, twelve projects totaling \$83,697,833 have been executed (disbursements were limited to the \$64,325,000). As of June 30, 2014, all projects were completed and \$1,963 of the project funds remains undisbursed. The transfer of the water and sewer utilities at Philadelphia Naval Business Center from PAID to the Water Department, including the projects outlined above, and occurred in November, 2009.

**NOTE 12: DEFERRED COMPENSATION PLAN**

The City offers its employees a deferred compensation plan in accordance with Internal Revenue Code section 457. As required by the Internal Revenue Code and Pennsylvania laws in effect at June 30, 2014, the assets of the plan are held in trust for the exclusive benefit of the participants and their beneficiaries. In accordance with GASB Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*, the City does not include the assets or activity of the plan in its financial statements.

**NOTE 13: ARBITRAGE REBATE**

The City has issued Water Revenue Bonds subject to Federal arbitrage requirements. Federal tax legislation requires the accumulated net excess of interest income on the proceeds of these issues over interest expense paid on the bonds be paid to the federal government at the end of a five-year period. The arbitrage liability was zero as of June 30, 2014 and 2013.

**PHILADELPHIA WATER DEPARTMENT**  
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**NOTE 14: DEBT PAYABLE**

A summary of changes in long-term debt obligations as of June 30, 2014 follows:

(In Thousands)

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Water and Sewer Revenue Bonds	\$ 1,620,275	\$ 293,170	\$ (215,385)	\$ 1,698,060	\$ 114,735
Pennvest Loans	139,504	23,577	(9,696)	153,385	10,565
Unamortized Bond Premium	70,608	28,349	(15,150)	83,807	-
Derivative Instrument Liability	8,565	-	(2,854)	5,711	-
Net Pension Liability	8,962	17,711	-	26,673	-
Other Non-Current Liabilities:					
Accrued Worker's Compensation	17,846	2,277	(3,309)	16,814	-
Accrued Legal Claims	4,387	5,642	(6,500)	3,529	-
Compensated Absences	9,972	1,957	(1,758)	10,171	-
Total Non-Current Liabilities	<u>\$ 1,880,119</u>	<u>\$ 372,683</u>	<u>\$ (254,652)</u>	<u>\$ 1,998,150</u>	<u>\$ 125,300</u>

An analysis of debt service requirements to maturity on the long-term obligations follows:

(In Millions of USD)

Years Ended June 30:	Principal Requirements	Interest Requirements	Total Debt Service Requirements
2015	\$ 125.3	\$ 79.6	\$ 204.9
2016	136.7	75.4	212.1
2017	124.8	68.4	193.2
2018	131.6	63.5	195.1
2019	86.8	59.1	145.9
2020-2024	381.5	241.7	623.2
2025-2029	292.1	172.3	464.4
2030-2034	279.7	106.4	386.1
2035-2039	161.0	52.5	213.5
2040-2044	131.9	16.6	148.5
Total	<u>\$ 1,851.4</u>	<u>\$ 935.5</u>	<u>\$ 2,786.9</u>

**PHILADELPHIA WATER DEPARTMENT  
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**NOTE 14: DEBT PAYABLE (CONTINUED)**

Pertinent information regarding long-term debt obligations outstanding is presented below:

Date of Issue	Amount of Original Issue	Purpose	Balance Outstanding at June 30, 2014
1997	\$78,500,000	Water and Wastewater Revenue Bonds, Variable Rate Series of 1997B, issued for various capital projects, to fund the Debt Reserve Account, and to pay the costs of issuance related to the bond issue at a variable rate.	\$63,800,000
1998	135,185,000	Water and Wastewater Revenue Refunding Bonds, Series of 1998, issued for defeasing a portion of the Series of 1993 Bonds, for defeasing a portion of the Fifteenth Series Bonds, and to pay the costs of issuance related to the bond issue at a rate of 5.25%.	38,025,000
1999	6,700,000	Pennsylvania Infrastructure Investment Authority Loan of 1999, issued for various capital projects at a rate of 1.41% - 2.73%.	410,107
2005	250,000,000	Water and Wastewater Revenue Bonds, Series of 2005A, issued for various capital projects, to fund the Debt Reserve Account of the Sinking Fund, and to pay the costs of issuance related to the bond issue at a rate of 3% - 5.25%.	117,250,000
2005	83,665,000	Water and Wastewater Revenue Refunding Bonds, Variable Rate Series of 2005B, issued for defeasing a portion of the Series of 1995 Bonds, and to pay the costs of issuance related to the bond issue at a variable rate.	67,175,000
2007	345,035,000	Water and Wastewater Revenue Refunding Bonds, Series of 2007A and 2007B, issued for defeasing the Series of 1997A and Series of 2001A Bonds, and to pay the costs of issuance related to the bond issue at a rate of 4% - 5%.	289,230,000

**PHILADELPHIA WATER DEPARTMENT  
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**NOTE 14: DEBT PAYABLE (CONTINUED)**

Date of Issue	Amount of Original Issue	Purpose	Balance Outstanding at June 30, 2014
2009	140,000,000	Water and Wastewater Revenue Bonds, Series of 2009A, issued for various capital projects, issued for funding the Debt Reserve Account of the Sinking Fund, and to pay the costs of issuance related to the bond issue at a rate of 4% - 5.75%.	140,000,000
2009	22,828,000	Pennsylvania Infrastructure Investment Authority Loan of 2009 (B), issued for various capital projects at a rate of 1.193% - 2.107%.	25,090,064
2009	35,667,000	Pennsylvania Infrastructure Investment Authority Loan of 2009 (C), issued for various capital projects at a rate of 1.193% - 2.107%.	36,230,899
2009	64,380,000	Pennsylvania Infrastructure Investment Authority Loan of 2009 (D), issued for various capital projects at a rate of 1.193% - 2.107%.	64,520,996
2010	8,111,000	Pennsylvania Infrastructure Investment Authority Loan of 2010 (B), issued for various capital projects at a rate of 1.193% - 2.107%.	27,133,256
2010	396,460,000	Water and Wastewater Revenue Refunding Bonds, Series of 2010A, issued for defeasing the Series of 2003 Bonds, issued for funding a payment to terminate the Series of 2003 Swap Agreement, for funding the required deposit into the Debt Reserve Account of the Sinking Fund, and to pay the costs of issuance related to the bond issue at a rate of 2% - 5%.	251,830,000
2010	185,000,000	Water and Wastewater Revenue Bonds, Series of 2010C, issued for funding a payment to terminate the Series of 2007 Swap Agreement, fund the required deposit into the Debt Reserve Account of the Sinking Fund, and to pay the costs of issuance related to the bond issue at a rate of 3% - 5%.	185,000,000

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 14: DEBT PAYABLE (CONTINUED)**

Date of Issue	Amount of Original Issue	Purpose	Balance Outstanding at June 30, 2014
2011	184,855,000	Water and Wastewater Revenue Bonds, Series of 2011A, and Water and Wastewater Revenue Refunding Bonds, Series of 2011B, issued for partially defeasing the Series of 2001A and Series of 2007A Bonds, for various capital projects, for funding of capitalized interest, for financing any required deposit into the Debt Reserve Account of the Sinking Fund, and to pay the cost of issuance related to the bond issue at a rate of 4% - 5%.	184,855,000
2012	70,370,000	Water and Wastewater Revenue Refunding Bonds, Series of 2012, issued for defeasing the Series of 2001A and 2001B Bonds and to pay the cost of issuance related to the bond issue at a rate of 1% - 5%.	67,725,000
2013	170,000,000	Water and Wastewater Revenue Bonds, Series of 2013A, issued to finance capital improvements, financing a deposit to the Debt Reserve Account, and to pay the cost of issuance related to the bond issue at a rate of 3% to 5.125%.	170,000,000
2014	123,170,000	Water and Wastewater Revenue Bonds, Series of 2014A, issued advance refund a portion of the Series of 2005A Bonds, to finance capital improvements, financing a deposit to the Debt Reserve Account, and to pay the cost of issuance related to the bond issue at a rate of 3% to 5%.	123,170,000
			<u>\$ 1,851,445,322</u>

In prior years, the Water Fund defeased certain bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Water Fund's financial statements. As of June 30, 2014, \$138.5 million of bonds outstanding were considered defeased. As of June 30, 2013 \$40.5 million of bonds outstanding were considered defeased.



**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 14: DEBT PAYABLE (CONTINUED)**

**Bond Issues**

In August 2013, the city issued Water and Wastewater Revenue Bonds Series 2013 A in the amount of \$170 million. Serial Bonds were issued in the amount of \$120 million with interest rates ranging from 3% to 5% and have a maturity date of 2023. Term Bonds were issued in the amount of \$50 million with an interest rate of 5.125% and mature in 2043. The proceeds of the bonds together with other available funds of the City's Water Department will be used to finance capital improvements to the City's Water and Wastewater systems, a deposit to the Debt Reserve account of the Sinking Fund and the cost of issuance relating to the Bonds.

In January 2014, the City issued Water and Wastewater Revenue Bonds Series 2014A in the amount of \$123.2 million. Serial Bonds were issued for \$93.2 million with interest rates ranging from 3.0% to 5.0% maturing July 1, 2027. Term bonds were issued in the amount of \$30 million with a 5.0% interest rate maturing July 1, 2043. The purpose of the bonds is to provide funds that will be used for the advance refunding of a portion of the City's outstanding Water and Wastewater Revenue Bonds, Series 2005A, capital improvements to the City's Water and Wastewater System, a deposit to the Debt Reserve Sinking Fund and the cost of issuance relating to the bonds. The aggregate difference in debt service between the refunding debt and the refunded debt is \$8.8 million. This refunding transaction resulted in a net economic gain of \$6.8 million.

**Pennvest Loans**

In July 2010, the City of Philadelphia Water Department received approval from the Pennsylvania Infrastructure Investment Authority ("PENNVEST") for the Green Infrastructure Project (Series 2010B), bringing the total financing from PENNVEST to \$214.9 million. During fiscal year 2014 and 2013, PENNVEST drawdowns totaled \$23.6 million and \$15.4 million, respectively, which represents an increase in bond issuances. The funding is through low interest loans of 1.193% during the construction period and for the first five years of amortization (interest only payment are due during the construction period up to three years) and 2.107% for the remaining fifteen years. Individual loan information as of June 30, 2014 is as follows:

Date	Series	Maximum Loan Amount	Approved Project Costs	Amount Requested through 6/30/14	Amount Received Yes/No
October 2009	2009B	\$42,886,030	\$42,339,199	\$28,790,697	Yes
October 2009	2009C	57,268,193	56,264,382	41,771,895	Yes
March 2010	2009D	84,759,263	84,404,754	71,703,769	Yes
July 2010	2010B	30,000,000	31,376,846	27,741,841	Yes
	Totals	<u>\$214,913,486</u>	<u>\$214,385,181</u>	<u>\$170,008,202</u>	

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 14: DEBT PAYABLE (CONTINUED)**

**Pennvest Loans (Continued)**

Individual loan information as of June 30, 2013 is as follows:

Date	Series	Maximum Loan Amount	Approved Project Costs	Amount Requested through 6/30/13	Amount Received Yes/No
October 2009	2009B	\$42,886,030	\$42,339,199	\$25,908,165	Yes
October 2009	2009C	57,268,193	56,264,382	40,338,440	Yes
March 2010	2009D	84,759,263	84,404,754	70,930,405	Yes
July 2010	2010B	30,000,000	31,376,846	9,254,100	Yes
	Totals	<u>\$214,913,486</u>	<u>\$214,385,181</u>	<u>\$146,431,110</u>	

**NOTE 15: DERIVATIVE INSTRUMENT**

**City of Philadelphia, 2005 Water & Sewer Swap**

*Objective:* In December, 2002, the City entered into a swaption that provided the City with an up-front payment of \$4.0 million. As a synthetic refunding of all or a portion of its 1995 Bonds, this payment approximated the present value savings, as of December 2002, of a refunding on May 4, 2005. The swaption gave Citigroup (formerly of Salomon Brothers Holding Company, Inc), the option to enter into an interest rate swap to receive fixed amounts and pay variable amounts.

*Terms:* Citigroup exercised its option to enter into a swap May 4, 2005, and the swap commenced on that date. Under the terms of the swap, the City pays a fixed rate of 4.53% and receives a variable payment computed as the actual bond rate or alternatively, 68.5% of one month LIBOR, in the event the average rate on the Bonds as a percentage of the average of one month LIBOR has exceeded 68.5% for a period of more than 180 days. Citigroup is currently paying 68.5% of one month LIBOR under the swap. The payments are based on an amortizing notional schedule (with an initial notional amount of \$86.1 million), and when added to an assumption for remarketing, liquidity costs and cost of issuance were expected to approximate the debt service of the refunded bonds at the time the swaption was entered into.

In May 2013, the City and Water Department converted the original variable rate bonds associated with the swap to an index-based rate, terminating the existing letter of credit in the process.

As of June 30, 2014, the swap had a notional amount of \$67.175 million and the associated variable rate bond had \$67.175 million principal amount. The bonds' variable rate coupons are based on the same index as the receipt on the swap. The bonds mature on August 1, 2018 and the related swap agreement terminates on August 1, 2018.

**PHILADELPHIA WATER DEPARTMENT  
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**NOTE 15: DERIVATIVE INSTRUMENT (CONTINUED)**

*Fair value:* As of June 30, 2014, the swap had a negative fair value of (\$5.71 million). This means that the Water Department would have to pay this amount if the swap terminated.

*Risk:* As of June 30, 2014, the City is not exposed to credit risk because the swap had a negative fair value. Should interest rates change and the fair value of the swap become positive, the City would be exposed to credit risk in the amount of the swap's fair value. Since the City is now receiving 68.5% of one month LIBOR, and paying 68.5% of one month LIBOR plus a fixed spread, the City is no longer exposed to basis risk, or tax risk. The swap includes an additional termination event based on credit ratings. The swap may be terminated by the City if the ratings of Citigroup or its Credit Support Provider fall below A3 or A-, or by Citigroup if the rating of the City's Water and Wastewater Revenue Bonds falls below A3 or A-. There are 30-day cure periods to these termination events. However, because the City's swap payments are insured by Assured Guaranty Municipal Corporation (formerly FSA), no termination event based on the City's Water and Wastewater Revenue Bond ratings can occur as long as Assured is rated at least A or A2.

As of June 30, 2014, rates were as follows:

<u>Terms</u>	<u>Rates</u>	
Interest Rate Swap		
Fixed payment to Citi under swap	Fixed	4.53000 %
Variable rate payment from Citi under swap	68.5% of 1-month Libor	(0.10631) %
Net interest rate swap payments		4.42369 %
Variable rate note coupon payments	68.5% of 1-month Libor + fixed spread	0.10631 %*
Synthetic interest rate on bonds		4.53000 %

*\*Excludes fixed spread, which is similar to the City's expected Letter of Credit costs on a comparable variable rate bond*

As of June 30, 2013, rates were as follows:

<u>Terms</u>	<u>Rates</u>	
Interest Rate Swap		
Fixed payment to Citi under swap	Fixed	4.53000 %
Variable rate payment from Citi under swap	68.5% of 1-month Libor	(0.13334) %
Net interest rate swap payments		4.39666 %
Variable rate note coupon payments	68.5% of 1-month Libor + fixed spread	0.13334 %*
Synthetic interest rate on bonds		4.53000 %

*\*Excludes fixed spread, which is similar to the City's expected Letter of Credit costs on a comparable variable rate bond*

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 15: DERIVATIVE INSTRUMENTS (CONTINUED)**

Swap payments and associated debt: As of June 30, 2014, debt service requirements of the variable rate debt and net swap payments for their term, assuming current interest rates remain the same, were as follows:

<b>Fiscal Year Ending June 30</b>	<b>Variable Rate Bonds</b>		<b>Interest Rate</b>	
	<b>Principal</b>	<b>Interest</b>	<b>Swaps, Net</b>	<b>Total Interest</b>
2015	\$ 15,535,000	\$ 71,415	\$ 2,971,612	\$ 3,043,027
2016	16,315,000	54,900	2,284,392	2,339,292
2017	17,145,000	37,555	1,562,668	1,600,223
2018	18,015,000	19,328	804,226	823,554
2019	165,000	175	7,299	7,474
<b>Total</b>	<b>\$ 67,175,000</b>	<b>\$ 183,373</b>	<b>\$7,630,197</b>	<b>\$7,813,570</b>

**NOTE 16: PENSION PLAN**

Effective with fiscal year 2014, the City implemented GASB Statement No. 67, *Financial Reporting for Pension Plans*. The new GASB required the City to re-evaluate its status as a single, multi, or employer defined benefit pension plan. The new statement defines a single employer as the primary government and its component units. However, the City's pension plan includes an entity, the Philadelphia Housing Development Corporation (PHDC), that is not a component unit. Therefore, beginning with fiscal year 2014, the City's pension plan meets the definition of a multi-employer plan. The City also maintains one single-employer defined pension plan for the Philadelphia Gas Works.

In June 2012, the GASB issued Statement No. 67, *Financial Reporting for Pension Plans*. This Statement replaces the requirements of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans* and Statement No. 50, *Pension Disclosures*. The statement establishes standards of financial reporting for separately issued financial reports and specifies the required approach for measuring a participating employer's pension liability. In most respects, the requirements for pension plan financial statements remain unchanged from the prior standards; however, the statements do require additional note disclosures including new schedules of required supplementary information.

Required Supplementary Information calculated in accordance with GASB Statement No. 25 is presented in audited financial statements of the respective pension plans. Copies of these financial statements may be obtained by contacting the Director of Finance of the City of Philadelphia.

The Pension Plans' financial statements are prepared using the accrual basis of accounting. Member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds of contributions are recognized when due and payable in accordance with the terms of the Fund.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 16: PENSION PLAN (CONTINUED)**

**A. Plan Administration**

The Philadelphia Board of Pensions and Retirement (the “Board”) administers the City of Philadelphia Public Employees Retirement System, a multiple employer defined benefit pension plan with a small but increasing defined contribution component, which provides pensions for all officers and employees of the City, as well as those of three quasi-governmental agencies (per applicable enabling legislation and contractual agreements). The Board was established by section 2-308 of the 1952 Philadelphia Home Rule Charter. Its actions in administering the Retirement System are governed by Title 22 of the Philadelphia Code.

**B. Plan Membership**

At July 1, 2013, the date of the most recent actuarial valuation, pension plan membership consisted of the following:

Actives	26,788
Terminated Vested	1,281
Disabled	4,152
Retirees	21,696
Beneficiaries	8,614
DROP	<u>2,427</u>
Total City Members	<u>64,958</u>
Annual Salaries	\$1,429,723,436
Average Salary per Active Member	\$53,372
Annual Retirement Allowances	\$676,634,789
Average Retirement Allowance	\$19,634

**C. Contributions**

Per Title 22 of the Philadelphia Code, members contribute to the System at various rates based on bargaining unit, uniform status, and entry date into the System. As of July 1, 2013 uniform employees will be contributing either 5.00%, 5.50%, or 6.00% of pensionable earnings; non-uniform employees will be contributing either 1.93%, 2.03%, 2.55%, or 6.00% of pensionable earnings; and elected employees will be contributing either 8.16% or 9.60% of pensionable earnings.

Employer contributions are made by the City throughout each fiscal year (which ends June 30) and by three (3) quasi-governmental agencies on a quarterly basis. These contributions, determined by an annual actuarial valuation report (“AVR”), when combined with plan member contributions, are expected to finance the cost of benefits earned by plan members during the year, with an additional amount to finance any unfunded accrued liability.

**PHILADELPHIA WATER DEPARTMENT  
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**NOTE 16: PENSION PLAN (CONTINUED)**

**C. Contributions (Continued)**

Within the AVR, two contribution amounts are determined based upon two different sets of rules for determining the way the unfunded actuarial liability is funded.

The first method is defined in accordance with Act 205 and defines the Minimum Municipal Obligation (“MMO”), which is the City’s minimum required contribution under Pennsylvania state law.

The second method is in accordance with the City’s Funding Policy which predates the Act 205 rules and calls for contributions that are greater than the MMO until the initial unfunded liability determined in 1984 is fully funded.

Under both funding methods there are two components: the normal cost and the amortized unfunded actuarial liability. The actuarial unfunded liability is the amount of the unfunded actuarial liability that is paid each year based upon the given or defined amortization periods. The amortization periods are different under the MMO and City’s Funding Policy.

**D. Funding Policy**

The initial July 1, 1985 unfunded actuarial liability (“UAL”) is amortized over 34 year ending June 30, 2019 with payments increasing at 3.3% per year, the assumed payroll growth. Other charges in the actuarial liability are amortized in level-dollar payments follows:

- Actuarial gains and losses – 20 years beginning July 1, 2009. Prior gains and losses were amortized over 15 years.
- Assumptions changes – 15 years beginning July 1, 2010. Prior changes were amortized over 20 years.
- Plan changes for active members – 10 years.
- Plan changes for inactive members – 1 year.
- Plan changes mandated by the State – 20 years.

In fiscal year 2014, the City and other employers’ contributions of \$533.2 million was less than the actuarially determined employer contribution (ADEC) of \$823.9 million. In the event that the City contributes less than the funding policy, an experience loss will be created that will be amortized in accordance with funding policy over 20 years.

The Schedule of Employer Contributions (based on the City’s Funding Policy) is included as Required Supplemental Information and provides a 6-year presentation of employer contributions.

**PHILADELPHIA WATER DEPARTMENT  
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**NOTE 16: PENSION PLAN (CONTINUED)**

**E. Minimum Municipal Obligation**

For the purposes of the MMO under Act 205 reflecting the fresh start amortization schedule, the July 1, 2009 UAL was “fresh started” to be amortized over 30 years ending June 30, 2039. This is a level dollar amortization of the UAL. All future amortization periods will follow the City’s Funding Policies as outlined above. In fiscal year 2014, the City and other employers’ contributions of \$553.2 million exceeded the Minimum Municipal Obligation of \$523.4 million.

**F. Benefits**

The Public Employees Retirement System provides retirement, disability, and death benefits according to the provisions of Title 22 of the Philadelphia Code. These provisions prescribe retirement benefit calculations, vesting thresholds, and minimum retirement ages, that vary based on bargaining unit, uniform/non-uniform status, and entry date into the System.

Non-uniform employees may retire at either age 55 with up to 80% of average final compensation (“AFC”) or may retire at either age 60 with up to 100% or 25% of AFC, depending on entry date into the System. Uniform employees may retire at either age 45 with up to 100% of AFC or age 50 with up to either 100% or 35% of AFC, depending on entry date into the System. Survivorship selections may result in an actuarial reduction to the calculated benefit.

Members may qualify for service-connected disability benefits regardless of length of service. Service-connected disability benefits are equal to 70% of a member’s final rate of pay, and are payable immediately without an actuarial reduction. These applications require approval by the Board.

Eligibility to apply for non-service-connected disability benefits varies by bargaining unit and uniform/non-uniform status. Non-service connected disability benefits are determined in the same manner as retirement benefits, and are payable immediately.

Service connected death benefits are payable to:

- 1) surviving spouse/life partner at 60% of final rate of pay plus up to 2 children under age 18 at 10% each of final rate of pay (maximum payout: 80%);
- 2) if no surviving spouse/life partner, up to 3 children under age 18 at 25% each of final rate of pay (maximum payout 75%); or
- 3) if no surviving spouse/life partner or children under age 18, up to 2 surviving parents at 15% each of final rate of pay (maximum payout 30%).

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 16: PENSION PLAN (CONTINUED)**

**F. Benefits (Continued)**

Non-service connected deaths are payable as a lump sum payment, unless the deceased was either vested or had reached minimum retirement age for their plan, in which case the beneficiary(s) may instead select a lifetime monthly benefit, payable immediately with an actuarial reduction.

A Pension Adjustment Fund (“PAF”) is funded with 50% of the excess earnings that are between 1% and 6% above the actuarial assumed earnings rate. Each year within sixty days of the end of the fiscal year, by majority vote of its members, the Board of Directors of the Fund (the “Board”) shall consider whether sufficient funds have accumulated in the PAF to support an enhanced benefit distribution (which may include, but is not limited to, a lump sum bonus payment, monthly pension payment increases, ad-hoc cost-of-living adjustments, continuous cost-of-living adjustments, or some other form of increase in benefits as determined by the Board) to retirees, their beneficiaries and their survivors. As of July 1, 2013, the date of the most recent actuarial valuation, there was \$1,096,608 in the PAF and the Board voted to make distributions of \$0 during the fiscal year ended June 30, 2014.

The Fund includes a Deferred Retirement Option Plan (DROP Plan). The DROP Plan allows a participant to declare that they will retire within 4 years. During the 4-year period, the City will make no further contributions for the participant. The participant would continue to work and to receive their salary; however, any increases would not be counted towards their pension benefit. During the 4-year period the individual participates in the DROP Plan, their pension benefits will be paid into an escrow account in the participant's name. After the 4-year period, the participant would begin to receive their pension benefits and the amount that has been accumulated in the escrow account in a lump sum payment. The balance in the DROP Plan as of June 30, 2014 is \$216.9 million.

The Annual Pension Cost and related percentage contributed for the three most recent fiscal years are as follows:

(Millions of Dollars)			
<b>Fiscal Year Ended June 30</b>	<b>Annual Pension Cost</b>	<b>Percentage Contributed</b>	<b>Net Pension Obligation</b>
2012	\$ 719.6	77.22%	\$ 243.9
2013	729.1	105.43%	204.3
2014	816.3	69.35%	454.5



**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 16: PENSION PLAN (CONTINUED)**

**F. Benefits (Continued)**

The actuarial valuation used to compute the current year's required contribution was performed as of July 1, 2013. Methods and assumptions used for that valuation include:

- the individual entry age actuarial cost method
- a ten-year smoothed market value method for valuing investments
- an annual investment rate of return of 7.85%
- projected annual salary increases based on new age based scale
- payroll growth rate is 3.3%
- no post-retirement benefit increases

Administrative costs of the Plan are paid out of the Plan's assets.

**G. Funding Status**

The following schedule shows the funding status based on the latest actuary report. The schedule of funding progress, which presents multiyear trend information about whether the actuarial value of plan assets is decreasing over time relative to the actuarial accrued liability for benefits, can be found in the Required Supplementary Information section immediately following the Notes to the Financial Statements.

(Millions of Dollars)

<b>Actuarial Valuation Date</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Accrued Liability (AAL)</b>	<b>Unfunded AAL (UAAL)</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAAL as a Percent of Covered Payroll</b>
	<b>(a)</b>	<b>(b)</b>	<b>(b - a)</b>	<b>(a / b)</b>	<b>(c)</b>	<b>(b - a) / c</b>
7/1/2011	\$ 4,489.1	\$ 9,487.5	\$ 4,998.4	47.32%	\$ 1,371.3	364.50%
7/1/2012	4,486.8	9,799.9	5,313.1	45.78%	1,372.2	387.20%
7/1/2013	4,799.3	10,126.2	5,326.9	47.39%	1,429.7	372.59%

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 16: PENSION PLAN (CONTINUED)**

**G. Funding Status (Continued)**

The City and other employers' annual pension cost and net pension obligation (NPO) for the Municipal Pension Plan for the current year were as follows:

	(Thousands of Dollars)
Annual Required Contribution (ARC)	\$ 823,885
Interest on Net Pension Obligation (NPO)	16,242
Adjustment to ARC	<u>(23,784)</u>
Annual Pension Cost	816,343
Contributions Made	<u>(566,179)</u>
Increase in NPO	250,164
NPO at beginning of year	<u>204,302</u>
NPO at end of year	<u>454,466</u>
Interest Rate	7.95%
15 Year Amortization Factor (EOY)	8.59%

The amount of increase in NPO related to the Water Department was \$17.7 million for fiscal year 2014.

**H. Derivative Instrument**

In 2010, the City of Philadelphia adopted GASB Statement No. 53 which addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. Derivative instruments such as swaps, options, futures and forwards are often complex financial arrangements used by governments to manage specific risks or to make investments. By entering into these arrangements, governments receive and make payments based on market prices without actually entering into the related financial or commodity transactions. Derivative instruments associated with changing financial and commodity prices result in changing cash flows and fair values that can be used as effective risk management or investment tools. Derivative instruments, however, also can expose governments to significant risks and liabilities.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 16: PENSION PLAN (CONTINUED)**

**H. Derivative Instrument (Continued)**

The City of Philadelphia Municipal Pension Fund (Pension Fund) enters into a variety of financial contracts which include options, futures, forwards and swap agreements to gain exposure to certain sectors of the equity and fixed income markets; collateralized mortgage obligations (CMO's); other forward contracts, and U.S. Treasury strips. The contracts are used primarily to enhance performance and reduce volatility of the portfolio. The Pension Fund is exposed to credit risk in the event of non performance by counterparties to financial instruments. The Pension Fund generally enters into transactions only with high quality institutions. Legal risk is mitigated through selection of executing brokers and review of all documentation. The Pension Fund is exposed to market risk, the risk that future changes in market conditions may make an instrument less valuable. Exposure to market risk is managed in accordance with risk limits set by Board approved guidelines, through buying or selling instruments or entering into offsetting positions. The notional or contractual amounts of derivatives indicate the extent of the Pension Fund's involvement in the various types and uses of derivative financial instruments and do not measure the Pension Fund's exposure to credit or market risks and do not necessarily represent amounts exchanged by the parties. The amounts exchanged are determined by reference to the notional amounts and the other terms of the derivatives.

The following table summarizes the aggregate notional or contractual amounts for the Pension Fund's derivative financial instruments at June 30, 2014:

<b>List of Derivatives Aggregated by Investment Type</b>					
Changes in Fair Value			Fair Value at June 30, 2014		
	Classification	Amount	Classification	Amount	Notional
<b>Investment Derivatives</b>					
<b>Forward Currency Contracts</b>	Net appreciation/(depreciation) in investments	\$ (1,981,432)	Accrued interest and other receivables	\$ (238,578)	\$ 150,909,330
<b>Futures</b>	Net appreciation/(depreciation) in investments	24,249	Accrued interest and other receivables	(3,524)	101
<b>Grand Totals</b>		<u>\$ (1,957,183)</u>		<u>\$ (242,102)</u>	<u>\$ 150,909,431</u>

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 16: PENSION PLAN (CONTINUED)**

**H. Derivative Instrument (Continued)**

A Derivatives Policy Statement identifies and allows common derivative instruments and strategies, which are consistent with the Investment Policy Statement of the City of Philadelphia Municipal Pension Fund. The guidelines identify transaction-level and portfolio-level risk control procedures and documentation requirements. Managers are required to measure and monitor exposure to counterparty credit risk. All counterparties must have credit ratings available from nationally recognized rating institutions such as Moody, Fitch, and S&P. The details of other risks and financial instruments in which the Fund involves are described below:

- 1) **Credit Risk:** The Pension Fund is exposed to credit risk on hedging derivative instruments that are in asset positions. To minimize its exposure to loss related to credit risk, it is the Pension Fund's policy to require counterparty collateral posting provisions in its non-exchange traded hedging derivative instruments. These terms require full collateralization of the fair value of hedging derivative instruments in asset positions (net of the effect of applicable netting arrangements) should the counterparty's credit rating fall below AA as issued by Fitch Ratings and Standard & Poor's or Aa as issued by Moody's Investors Service. Collateral posted is to be in the form of U.S. Treasury securities held by a third-party custodian. The City has never failed to access collateral when required.

It is the Pension Fund's policy to enter into netting arrangements whenever it has entered into more than one derivative instrument transaction with counterparty. Under the terms of these arrangements, should one party become insolvent or otherwise default on its obligations, close-out netting provisions permit the non-defaulting party to accelerate and terminate all outstanding transactions and net the transactions' fair values so that a single sum will be owed by, or owed to, the non-defaulting party.

- 2) **Swap Agreements:** Swap agreements provide for periodic payments at predetermined future dates between parties based on the change in value of underlying securities, indexes or interest rates. During the year ended June 30, 2012 the Fund entered into interest rate swaps. Under the receive fixed interest rate type swap arrangements, the Fund receives the fixed interest rate on certain equity or debt securities or indexes in exchange for a fixed charge. There were not any total receive fixed interest Swaps this year. On its pay-variable, received-fixed interest rate swap, as LIBOR increases, the Fund's net payment on the swap increases. Alternatively, on its pay-fixed, receive-variable interest rate swap, as LIBOR or the SIFMA swap index decreases, the Fund's net payment on the swap increases.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 16: PENSION PLAN (CONTINUED)**

**H. Derivative Instrument (Continued)**

- 3) **Future Contracts:** Future contracts are types of contracts in which the buyer agrees to purchase and the seller agrees to make delivery of a specific financial instrument at a predetermined date and price. Gains and losses on futures contracts are settled daily based on a notional (underlying) principal value and do not involve an actual transfer of the specific instrument. Futures contracts are standardized and are traded on exchanges. The exchange assumes the risk that counterparty will not pay and generally requires margin payments to minimize such risk. In addition, the Fund enters into short sales, sales of securities it does not presently own, to neutralize the market risk of certain equity positions. Initial margin requirements on futures contracts and collateral for short sales are provided by investment securities pledged as collateral and by cash held by various brokers. Although the Fund has the right to access individual pledged securities, it must maintain the amount pledged by substituting other securities for those accessed. The realized gain from Future contracts was \$749,289.
- 4) **Forward contracts:** The Fund is exposed to basis risk on its forward contract because the expected funds purchase being hedged will price based on a pricing point different than the pricing point at which the forward contract is expected to settle. The realized loss from Forward contracts was \$(1,913,361).
- 5) **Termination risk:** The Fund or its counterparties may terminate a derivative instrument if the other party fails to perform under the terms of the contract. In addition, the Fund is exposed to termination risk on its receive-fixed interest rate swap. The Fund is exposed to termination risk on its rate cap because the counter-party has the option to terminate the contract if the SIFMA swap index exceeds 12 percent. If at the time of termination, a hedging derivative instrument is in a liability position, the city would be liable to the counter-party for a payment equal to the liability, subject to netting arrangements.
- 6) **Rollover Risk:** The Fund is exposed to rollover risk on hedging derivative instruments that are hedges of debt that mature or may be terminated prior to the maturity of the hedged debt. When these hedging derivative instruments terminate, or in the case of a termination option, if the counterparty exercises its option, the Fund will be re-exposed to the risks being hedged by the hedging derivative instrument.

**I. Summary of Significant Accounting Policies**

Financial statements of the Fund are prepared using the accrual basis of accounting. Member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds of contributions are recognized when due and payable in accordance with the terms of the Fund. Investments are valued as described in Note 2I.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 17: OTHER POST EMPLOYMENT BENEFITS**

**A. Plan description**

The City of Philadelphia self-administers a single employer, defined benefit plan and provides health care for five years subsequent to separation for eligible retirees. Certain union represented employees may defer their coverage until a later date, but the amount that the City pays for their health care is limited to the amount that the City would have paid at the date of their retirement. The City also provides lifetime insurance coverage for all eligible retirees. Firefighters are entitled to \$7,500 coverage and all other employees receive \$6,000 in coverage. The plan does not issue stand alone financial statements, and the accounting for the plan is reported within the financial statements of the City of Philadelphia.

**B. Funding Policy**

The City funds its retiree benefits on a pay-as-you-go basis. To provide health care coverage, the City pays a negotiated monthly premium for retirees covered by union contracts and is self insured for non-union employees. For fiscal year 2014, the City paid \$67.1 million for retiree healthcare.

**C. Annual OPEB Cost and Net OPEB Obligation**

The City's annual other post employment benefit (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, which if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities over a period not to exceed thirty (30) years. The following table shows the components of the City's annual OPEB cost for the year, the amount actually contributed to the plan and changes in the net OPEB obligation:

	(Thousands of Dollars)
Annual Required Contribution	\$ 128,619
Interest on Net OPEB Liability	7,068
Adjustment to Annual Required Contribution	<u>(6,369)</u>
Annual OPEB Cost	129,318
Payments Made	<u>(67,100)</u>
Increase in Net OPEB Obligation	62,218
Net OPEB Obligation at beginning of year	<u>166,315</u>
Net OPEB Obligation at end of year	<u>\$ 228,533</u>

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 17: OTHER POST EMPLOYMENT BENEFITS (CONTINUED)**

**C. Annual OPEB Cost and Net OPEB Obligation (Continued)**

The City of Philadelphia's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for the fiscal year ended June 30, 2014 was as follows:

(Thousands of Dollars)

<b>Fiscal Year Ended</b>	<b>Annual OPEB Cost</b>	<b>Percentage of Annual OPEB Contributed</b>	<b>Net OPEB Obligation</b>
6/30/2014	\$ 129,318	52%	\$ 228,533
6/30/2013	114,392	50%	166,314
6/30/2012	105,369	72%	109,019

**D. Funded Status and Funding Progress**

As of July 1, 2013, the most recent actuarial valuation date, the City is funding OPEB on a pay as you go basis and accordingly, the unfunded actuarial accrued liability for benefits was \$1.7 billion. The covered annual payroll was \$1.417 billion and the ratio of the UAAL to the covered payroll was 120.2%.

The required schedule of funding progress immediately following the notes to the financial statements presents multi-year trend information about whether the actuarial value of the plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

The projections of future benefit payments for an ongoing plan obligation involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Amounts determined regarding the funded status of the obligation and the 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.

**E. Actuarial Methods and Assumptions**

Projections of costs for financial reporting purposes are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing costs between the employer and plan members to that point.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 17: OTHER POST EMPLOYMENT BENEFITS (CONTINUED)**

**E. Actuarial Methods and Assumptions (Continued)**

Costs were determined according to the individual entry age actuarial cost method with the attribution period ending at each decrement age. This is consistent with the cost method used for the City of Philadelphia Municipal Retirement System. The City uses a level percent open approach as its method of amortization. Unfunded liabilities are funded over a 30 year period as a level percentage of payroll, which is assumed to increase at a compound annual rate of 4.25% per year. The actuarial assumption included a 7.95% compound annual interest rate on the City's general investments. The current plan incorporates the following assumptions: no post-retirement benefit increases since last year; a 7.85% Investment Rate of Return, a 3.30% Rate of Salary increases; and, a 4% Ultimate Rate of Medical Inflation.

**NOTE 18: CLAIMS, LITIGATION, AND CONTINGENCIES**

Generally, claims against the City are payable out of the General Fund, except claims against the City Water Department, City Aviation Division, or Component Units which are paid out of their respective funds and only secondarily out of the General Fund which is then reimbursed for the expenditure. Unless specifically noted otherwise, all claims hereinafter discussed are payable out of the Water Fund.

The Act of October 5, 1980, P.L. 693, No. 142, known as the "Political Subdivision Tort Claims Act," established a \$500,000 aggregate limitation on damages arising from the same cause of action, transaction, occurrence, or series of causes of action, transactions or occurrences with respect to governmental units in the Commonwealth such as the City. The constitutionality of that aggregate limitation has been upheld by the United States Supreme Court. There is no such limitation under federal law.

Various claims have been asserted against the Water Department and in some cases lawsuits have been instituted. Many of these claims are reduced to judgment or otherwise settled in a manner requiring payment by the Water Department. As of June 30, 2014 and 2013, the aggregate estimate of loss deemed to be probable is \$20.3 million and \$22.2 million, respectively. This amount has been included on the Statement of Net Position under Other Long-Term Liabilities.

In addition to the above, there are other lawsuits against the Water Department in which some amount of loss is reasonably possible. The aggregate estimate of the loss, which could result if unfavorable legal determinations were rendered against the Water Department with respect to these lawsuits, is \$9.2 million and \$9.4 million as of June 30, 2014 and 2013, respectively.



**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 19: LONG TERM AGREEMENTS**

The Water Department has entered into several long term agreements with third parties through the Philadelphia Municipal Authority as follows:

**A. Automatic Meter Reading**

In September 1997, the Water Department and the Water Revenue Bureau began the implementation of the Automatic Meter Reading Program (the “AMR Program”) involving the replacement of all residential water meters with new meters equipped with radio transmitter meter reading devices (“ERT”). Installation commenced on schedule on September 11, 1997. By June 30, 2012, more than 482,841 new meters had been installed. The AMR Program significantly reduced the costs of meter reading and related support. As of June 30, 2014, more than 99.5% of the Water Department’s customers have AMR meters, drastically improving the Water Department’s ability to initiate and enforce collection of delinquent accounts. From 2011 through 2013, as required in the long-term meter reading contract, the service provider (ITRON) conducted battery replacement of the vast majority of customer reading endpoint devices (ERTs), thus enabling the battery capability of the existing population through 2025. The Water Department is also working on the purchase and installation of upgraded AMR devices for all commercial customers that have ERTs. The AMR Program agreement term ends in 2017. The Department has two one-year renewal options.

Under the agreement ITRON is paid a fixed amount for each monthly meter reading actually obtained. The Water Department paid ITRON, through the Philadelphia Municipal Authority (“PMA”), \$1,984,362 and \$1,964,275 in Fiscal Year 2014 and Fiscal Year 2013, respectively for meter reads. Additionally, the Water Department paid ITRON, through PMA, \$1,809,838 and \$1,732,516 in Fiscal Year 2014 and Fiscal Year 2013, respectively, for the purchase of meters.

**B. Biosolids Treatment and Utilization**

The City is required by Federal and Commonwealth law, administered by the U.S. Environmental Protection Agency (“EPA”) and the Pennsylvania Department of Environmental Protection (“PADEP”), respectively, to treat and dispose of biosolids captured during wastewater treatment at the City’s Water Pollution Control Plants (“WPCP’s”). Biosolids from the three WPCP is treated at the Biosolids Recycling Center (“BRC”). The BRC had historically produced two grades of biosolids, as defined by state and federal regulations. These were Class A biosolids compost and Class B dewatered biosolids cake. Class B biosolids were used on farmlands and at mine reclamation sites and co-disposed with trash at municipal solid waste landfills. Class A compost, which was produced at the BRC until October 2007, was put to a variety of local and regional uses, including garden and horticultural applications and recreation sites.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 19: LONG TERM AGREEMENTS (CONTINUED)**

**B. Biosolids Treatment and Utilization (Continued)**

Biosolids processing and distribution is governed at the national level by EPA regulations published at 40 CFR Part 503 regulations in February 1993 (the “Part 503 Regulations”). The Part 503 Regulations require, among other things, certain record keeping and monitoring procedures and compliance with technical standards for pathogen reduction, vector attraction reduction and pollutant limits. These regulations are self-implementing and directly enforceable, in that the EPA can initiate enforcement actions for non-compliance even in the absence of the EPA’s issuance of permits under the National Pollutant Discharge Elimination System (“NPDES”) permitting program. The Water Department is in full compliance with the technical standards in the Part 503 Regulations.

While the Water Department has administered a successful Class A and B biosolids program over the last 25 years, the nation has witnessed continuing health and environmental concerns raised by the public with Class B biosolids recycling. As such, in the summer of 2003, the Water Department began a process to move to an entirely Class A biosolids process, which could operate in Philadelphia without odors. It entered into a contract with the engineering consultant firm Camp, Dresser & McKee to assist with the procurement of facilities and services for Philadelphia to operate the dewatering station for 20 years and to construct new facilities to produce Class A biosolids products.

Philadelphia Biosolids Services, LLC (“PBS”) submitted a proposal on November 24, 2004. PBS offered to build a pair of sludge dryers to produce Class A pellets. On June 19, 2008, City Council passed enabling legislation to allow the proposed contract with PBS to proceed. Mayor Nutter approved the contract with PBS in October 2008 and PBS has been operating the facility since October 13, 2008. The Water Department entered into a contract and lease with the Philadelphia Municipal Authority (“PMA”) to operate the Water Department’s existing BRC, including a dewatering station, and to construct new thermal drying facilities to produce Class A biosolids pellets. The contract term is up to 25 years, including a five-year renewal option. PMA has contracted with PBS for these services.

The contract included a provision for an interim period of up to five years, during which PBS took over operation of the existing Biosolids Recycling Center. Within the first four years, PBS financed \$68,275,000 through the Pennsylvania Economic Development Finance Authority, designed, built and now owns and operates a thermal drying facility that handles all of the sludge processed by the Water Department and makes a Class A product in the form of pellets that is used as fertilizer and has potential as a fuel. PBS is responsible for the disposition of the Class A pellets, thus relieving the Water Department of this burden. The Class A period of operation will last 20 years with a five-year renewal at the option of the Water Department.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 19: LONG TERM AGREEMENTS (CONTINUED)**

**B. Biosolids Treatment and Utilization (Continued)**

When the contract was executed, the Water Department transferred the remaining 60 employees at this facility to other assignments. Subsequently, the Water Department has also transferred to other units, certain vehicles and equipment that had been part of the existing BRC operation but were no longer needed by the contractor. At this time, most of the fixed assets associated with the facility, except for those related to the discontinued composting operations, remain in service (see Note 7).

Payments for the facility are made to PBS through PMA. Fiscal year 2012 payments totaled \$21,835,872, which included partial year operation of the new Class A pellet facility. Fiscal year 2013 was the first full year of operation of the Class A facility with payments totaling \$21,275,441. Fiscal year 2014 payments for the facility totaled \$20,364,249.

**C. Northeast Water Pollution Control Plant Digester Gas Cogeneration Facility**

On December 23, 2011, the Department entered into a contract for the construction and leaseback of a 5.6 Megawatt digester gas (biomethane, which is a renewable energy source) cogeneration facility at the Water Department's Northeast WPCP. This project is expected to produce over 40 million kWh per year. The facility was placed into operation on December 12, 2013.

The parties to this agreement, which will bring green power to the Northeast WPCP, are the Philadelphia Water Department ("City"), Ameresco Energy ("Developer"), and Bank of America. The Developer will build the biogas combined heat and power system that runs on methane gas produced on site and incorporates a small amount of natural gas to optimize engine performance. Bank of America, the facility owner and lessor, has formed a special purpose entity "BAL Biogas 1" and the City pays a monthly fee through PMA, the lessee. The Philadelphia Water Department operates the facility. Under a separate but related agreement Ameresco Energy will maintain the equipment. The structure of the deal allows for Bank of America to apply for the IRS code section 1603 grant in lieu of tax credit under the ARRA and ITC rules that amount to 30% of the qualified cost.

In fiscal year 2014, the Water Department paid Bank of America, through PMA, lease payments of \$2,427,767, maintenance fees of \$1,291,352, and legal, administrative, and other miscellaneous fees of \$54,700. Maintenance fees vary per year based on the amount of work required and is paid separately.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 19: LONG TERM AGREEMENTS (CONTINUED)**

**D. Laurel Street Combined Sewer Overflow**

On June 7, 2011 the City of Philadelphia entered into an Amended and Restated Development and Tax and Claim Settlement Agreement (the “agreement”) with Sugarhouse HSP Gaming, L.P. (HSP). In accordance with the agreement, HSP is required to fund development and expansion of the Laurel Street combined sewer overflow. In compensation for this construction, HSP is allotted a five year credit against its real estate taxes and settlement payments otherwise due to the City of Philadelphia. This credit is equal to 28 percent of the amount expended on the Laurel Street Combined Sewer Overflow project. If the credit exceeds the amount of real estate taxes and settlement payments due to the City, the credit carries over to the following year.

As the Laurel Street Combined Sewer Overflow is a capital asset of the Water Department, the Water Department is required to transfer to the General Fund of the City the amount of this credit. This credit is approximately \$3.5 million per year during fiscal year 2014 through 2018.

**NOTE 20: COMBINED SEWER OVERFLOW PROGRAM**

The present NPDES permits require the Water Department to implement a combined sewer overflow program. In older sections of the City, both wastewater and stormwater are conveyed in one pipe to the sewage treatment plant. This is known as a combined system. During certain rain events, the additional stormwater exceeds the capacity of the collection system and/or wastewater treatment plant and causes an overflow. The excess stormwater/wastewater mix known as combined sewer overflow (“CSO”) discharges directly to local waterways. The Water Department has 164 CSO points in its collection system.

Since 1997, the Water Department has been committed to restoring the region’s waterways to fishable, swimmable, and beautiful rivers and streams that are life sustaining and are an amenity to nearby communities. The PADEP and the Water Department signed a consent order and agreement dated as of June 1, 2011 (“COA”) that allowed the Water Department to officially embark on the implementation of its landmark strategy known as the *Green City, Clean Waters Program*. Pursuant to the *Green City, Clean Waters Program*, the Water Department will spend approximately \$2.4 billion over the next 25 years (\$1.2 billion in 2009 dollars) to use green technologies to substantially mitigate CSOs and enhance the quality of local waterways. The plan also includes wastewater treatment facility enhancements and pipe renewal and replacement.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 20: COMBINED SEWER OVERFLOW PROGRAM (CONTINUED)**

The COA complies with Clean Water Act requirements by adopting the presumption approach to CSO control. The goal under the presumption approach is to eliminate or remove the mass of pollutants that otherwise would be removed by the capture of 85% by volume of the combined sewage otherwise collected in the City's combined sewer system during precipitation events. To ensure this ultimate goal is met, the COA requires that interim water quality milestones at years 5, 10, 15, and 20 of the COA. The interim milestones require the City to achieve specific targets in four categories: (1) Total Greened Acres; (2) Overflow Reduction Volume; (3) Miles of Interceptor Lined; (4) WPCP Upgrades: Design and Construction.

The COA includes financial protections in the event that the costs of complying with the COA exceed the Water Department's projections. Should COA costs increase to extent that the wastewater component of a customer's bill exceed 2.27% of the median household income the City may petition the PADEP for an extension of time to satisfy the COA so that the financial burden does not become excessive on ratepayers.

The COA also includes significant penalties for noncompliance with the 5 year milestone targets. Penalties start at \$25,000 per month for each violation (for the first six months) and increase up to \$100,000 per month for uncured violations of 13 months or more.

**NOTE 21: PLEDGE OF REVENUES**

Section 4.02 and 4.04 of the Water bond ordinance of 1989, as amended in 1993, which authorized the issuance of Water and Sewer Revenue Bonds, pledges and assigns to the Fiscal Agent for the security and payment of all bonds, a lien on and security interest in all project revenues and amounts on deposit in or standing to the credit of the: 1) Revenue Fund; 2) Sinking Fund et.al.; 3) Subordinated Bond Fund; 4) Rate Stabilization Fund; 5) Residual Fund; and 6) Construction Fund et al. The fiscal agent shall hold and apply the security interest granted in trust for the holders of bonds listed above without preference, priority, or distinction; provided however, that the pledge of this ordinance may also be for the benefit of a credit facility and qualified swap, or any other person who undertakes to provide moneys for the account of the City for the payment of principal or redemption price and interest on any series of bonds (other than subordinated bonds), on an equal and ratable basis with bonds, to the extent provided by any Supplemental Ordinance or Determination. The amount of this pledge is the equal to the remaining principal and interest outstanding on the Water and Sewer Revenue Bonds. The purpose for the debt secured by the pledge can be found in Note 14 to the financial statements.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
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**NOTE 21: PLEDGE OF REVENUES (CONTINUED)**

The following chart displays information related to the pledge as of June 30, 2014:

	<u>Water and Sewer Revenue Bonds</u>
Pledged Revenue Required for Principal and Interest Payments	\$2,786.9 million
Term of Pledge	2044
Percentage of Revenue Pledged	100%
Current Year Pledged Revenue	\$644.2 million
Current Year Principal and Interest Paid	\$302.6 million

The following chart displays information related to the pledge as of June 30, 2013:

	<u>Water and Sewer Revenue Bonds</u>
Pledged Revenue Required for Principal and Interest Payments	\$2,613.2 million
Term of Pledge	2041
Percentage of Revenue Pledged	100%
Current Year Pledged Revenue	\$626.8 million
Current Year Principal and Interest Paid	\$287.2 million

**NOTE 22: RISK MANAGEMENT**

The City is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City (except for Aviation Fund operations, the Municipal Authority and PICA) is self-insured for fire damage, casualty losses, public liability, Workers' Compensation and Unemployment Compensation. The Aviation Fund is self-insured for Workers' Compensation and Unemployment Compensation and insured through insurance carriers for other coverage.

The City covers all claim settlements and judgments, except for those discussed above, out of the resources of the fund associated with the claim. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include: an estimate of claims that have been incurred but not reported; the effects of specific, incremental claims adjustment expenditures, salvage, and subrogation; and unallocated claims adjustment expenditures.

**PHILADELPHIA WATER DEPARTMENT  
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**NOTE 22: RISK MANAGEMENT (CONTINUED)**

At June 30, the amount of these liabilities was \$349.3 million for the City. This liability is the City's best estimate based on available information. Changes in the reported liability since June 30, 2012 resulted from the following:

Amounts in Millions of USD				
Fiscal Years Ending June 30	Beginning Liability	Current Year Claims and Changes in Estimates	Claim Payments	Ending Liability
2012	\$353.5	\$102.1	\$(99.8)	\$355.8
2013	355.8	101.6	(101.3)	356.1
2014	356.1	274.2	(281.0)	349.3

The City's Unemployment Compensation and Workers' Compensation coverages are provided through its General Fund. Unemployment Compensation and Workers' Compensation coverages are funded by a pro rata charge to the various funds. Payments for the year were \$3.2 million for Unemployment Compensation claims and \$62.2 million for Workers' Compensation claims.

The City's estimated outstanding workers' compensation liabilities are \$280.2 million discounted at 3.5%. On an undiscounted basis, these liabilities total \$367.5 million. These liabilities include provisions for indemnity, medical and allocated loss adjustment expense (ALAE). Excluding the ALAE, the respective liabilities for indemnity and medical payments relating to workers' compensation total \$251.7 million (discounted) and \$330.9 million (undiscounted). The Water Department's accrued liability for workers compensation was \$20.3 million and \$22.2 million at June 30, 2014 and 2013, respectively.

During the last five (5) fiscal years, no claim settlements have exceeded the level of insurance coverage for operations using third party carriers. None of the City's insured losses have been settled with the purchase of annuity contracts.

**PHILADELPHIA WATER DEPARTMENT  
NOTES TO THE FINANCIAL STATEMENTS  
JUNE 30, 2014**

**NOTE 23: RESTATEMENT OF NET POSITION / CHANGE IN ACCOUNTING PRINCIPLE**

The following restatement of net position was necessary to properly reflect the adoption of GASB Statement No. 65, *“Items Previously Reported as Assets and Liabilities”*:

	(Amounts in Thousands)
Net Position, Beginning Balance of Fiscal Year 2013, as Previously Stated	\$ 865,320
Expense of Bond Issuance Costs due to the adoption of GASB Statement No. 65	<u>(56,373)</u>
Net Position, Beginning Balance of Fiscal Year 2013, as Restated	\$ <u>808,947</u>

**NOTE 24: SUBSEQUENT EVENTS**

The Water Department self-insures up to \$6.5 million for claims and damages under litigation. As of January 31, 2015, the amount of self-insurance available was \$0.

Through January 2015, drawdowns totaling \$0.4 million represent new loans from the Pennsylvania Infrastructure Investment Authority (“PENNVEST”).



## **Required Supplementary Information**

## BUDGETARY COMPARISON SCHEDULE

Water Operating Fund

For the Fiscal Year Ended June 30, 2014

(Legally Enacted Basis)

(Thousands of Dollars)

<u>Revenues</u>	<u>Budgeted Amounts</u>		<u>Actual</u>	<u>Final Budget to Actual Positive (Negative)</u>
	<u>Original</u>	<u>Final</u>		
Locally Generated Non-Tax Revenue	\$ 606,789	\$ 603,747	\$ 607,107	\$ 3,360
Revenue from Other Governments	1,350	850	1,946	1,096
Revenue from Other Funds	79,941	52,752	33,966	(18,786)
<b>Total Revenues</b>	<b>\$ 688,080</b>	<b>\$ 657,349</b>	<b>\$ 643,019</b>	<b>\$ (14,330)</b>
<u><b>Expenditures and Encumbrances</b></u>				
Personal Services	116,125	116,065	108,957	7,108
Pension Contributions	59,200	61,486	60,755	731
Other Employee Benefits	43,330	41,044	41,044	-
Sub-Total Employee Compensation	218,655	218,595	210,756	7,839
Purchase of Services	157,164	157,224	133,942	23,282
Materials and Supplies	49,002	48,881	45,946	2,935
Equipment	4,964	5,085	3,468	1,617
Contributions, Indemnities and Taxes	6,602	6,602	6,037	565
Debt Service	205,355	205,355	204,646	709
Payments to Other Funds	58,456	58,456	75,660	(17,204)
Advances and Other Miscellaneous Payments	9,882	9,882	-	9,882
<b>Total Expenditures and Encumbrances</b>	<b>710,080</b>	<b>710,080</b>	<b>680,455</b>	<b>29,625</b>
<b>Operating Surplus (Deficit) for the Year</b>	<b>\$ (22,000)</b>	<b>\$ (52,731)</b>	<b>\$ (37,436)</b>	<b>\$ 15,295</b>
 Fund Balance Available, July 1, 2013	 -	 -	 -	 -
<u><b>Operations in Respect to Prior Fiscal Years</b></u>				
Commitments Cancelled - Net	22,000	22,000	37,436	15,436
Prior Period Adjustments	-	-	-	-
 Adjusted Fund Balance, July 1, 2013	 22,000	 22,000	 37,436	 15,436
 <b>Fund Balance Available, June 30, 2014</b>	 <b>\$ -</b>	 <b>\$ (30,731)</b>	 <b>\$ -</b>	 <b>\$ 30,731</b>

CITY OF PHILADELPHIA  
PENSION PLANS AND OTHER POST EMPLOYMENT BENEFITS  
SCHEDULE OF FUNDING PROGRESS  
FISCAL YEAR ENDED JUNE 30, 2014

(Amounts in Millions of USD)

<b>Actuarial Valuation Date</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Accrued Liability (AAL)</b>	<b>Unfunded AAL (UAAL)</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAAL as a Percentage of Covered Payroll</b>
	(a)	(b)	(b - a)	(a / b)	(c)	(b - a) / c
<b><u>City of Philadelphia Municipal Pension Plan</u></b>						
07/01/2008	\$4,623.6	\$8,402.2	\$3,778.6	55.03%	\$1,456.5	259.43%
07/01/2009	4,042.1	8,975.0	4,932.9	45.04%	1,463.3	337.11%
07/01/2010	4,230.9	9,317.0	5,086.1	45.41%	1,421.2	357.87%
07/01/2011	4,489.1	9,487.5	4,998.4	47.32%	1,371.3	364.50%
07/01/2012	4,486.8	9,799.9	5,313.1	45.78%	1,372.2	387.20%
07/01/2013	4,799.3	10,126.2	5,326.9	47.39%	1,429.7	372.59%
<b><u>City of Philadelphia Other Post Employment Benefits</u></b>						
07/01/2008	\$-	\$1,156.0	\$1,156.0	0.00%	\$1,456.5	79.37%
07/01/2009	-	1,119.6	1,119.6	0.00%	1,461.7	76.60%
07/01/2010	-	1,169.5	1,169.5	0.00%	1,419.5	82.39%
07/01/2011	-	1,212.5	1,212.5	0.00%	1,469.2	82.53%
07/01/2012	-	1,511.9	1,511.9	0.00%	1,371.6	110.23%
07/01/2013	-	1,703.6	1,703.6	0.00%	1,416.9	120.23%

## **Other Supplementary Information**

## CITY OF PHILADELPHIA WATER DEPARTMENT

## BONDED DEBT FOR THE FISCAL YEAR ENDED JUNE 30, 2014

(Thousands of Dollars)

						FISCAL YEAR 2015		
						DEBT		
ORIGINAL AUTHORIZATION			Outstanding June 30, 2014	Maturities	Interest Rates	Service Interest	Principal Requirements	Outstanding June 30, 2015
Series	Date	Issued						
Revenue Bonds:								
Series 1997 (B)	11/25/97	100,000	63,800	8/2007 to 8/2027	Variable	53	3,400	60,400
Series 1998	12/25/98	135,185	38,025	12/2011 to 12/2014	5.25	998	38,025	
Series 2005 (A)	05/04/05	250,000	117,250	7/2007 to 7/2035	3.250 to 5.250	5,724	5,535	111,715
Series 2005 (B)	05/04/05	86,105	67,175	8/2007 to 8/2018	Variable	2,691	15,535	51,640
Series 2007 (A)	05/04/07	191,440	137,010	8/2007 to 8/2027	4.00 to 5.00	6,551	-	137,010
Series 2007 (B)	05/04/07	153,595	152,220	11/2007 to 11/2031	4.00 to 5.00	6,923	245	151,975
Series 2009 (A)	05/21/09	140,000	140,000	1/2017 to 1/2036	5.15 to 5.25	7,294	-	140,000
Series 2010 (A)	04/15/10	396,460	251,830	6/2010 to 6/2019	0.500 to 4.110	12,023	49,275	202,555
Series 2010 (C)	08/05/10	185,000	185,000	8/2016 to 8/2030	2.530 to 4.560	9,022	-	185,000
Series 2011 (A)	11/16/11	135,000	135,000	1/2036 to 1/2041	4.50 to 5.00	6,737	-	135,000
Series 2011 (B)	11/16/11	49,855	49,855	11/2016 to 11/2026	4.00 to 5.00	2,461	-	49,855
Series 2012	11/01/12	70,370	67,725	11/2013 to 11/2028	1.00 to 5.00	3,305	2,720	65,005
Series 2013 (A)	08/22/13	170,000	170,000	1/2017 to 1/2043	3.00 to 5.125	8,472	-	170,000
Series 2014 (A)	01/23/14	30,000	30,000	7/2041 to 7/2043	5.00	1,408	-	30,000
Series 2014 (R)	01/23/14	93,170	93,170	7/2016 to 7/2027	3.00 to 5.00	4,219	-	93,170
Pennvest - 1999	04/30/00	6,700	410	7/2007 to 4/2019	1.41 to 2.73	10	80	330
Pennvest - 2009 (B)	10/14/09	28,791	25,090	7/2013 to 6/2033	1.193 to 2.107	288	2,124	22,966
Pennvest - 2009 (C)	10/14/09	41,772	36,231	7/2013 to 6/2033	1.193 to 2.107	417	2,803	33,428
Pennvest - 2009 (D)	03/31/10	71,704	64,521	7/2013 to 6/2033	1.193 to 2.107	747	4,164	60,357
Pennvest - 2010 (B)		27,742	27,133			316	1,394	25,739
Total Revenue Bonds		2,362,889	\$ 1,851,445			79,659	125,300	\$ 1,726,145
Total Bonded Debt			\$ 1,851,445			\$ 79,659	\$ 125,300	\$ 1,726,145

## ANNUAL BONDED DEBT SERVICE REQUIREMENT:

Fiscal Year	Interest	Principal	Total
2015	79,659	125,300	204,959
2016	75,377	136,733	212,110
2017	68,402	124,808	193,210
2018	63,533	131,558	195,091
2019	59,079	86,827	145,906

The First Series through the Thirteenth were refunded.

Capitalized Interest added to Construction in Progress in Fiscal 2014 was \$3,926,863.  
Interest Expense was reduced by the same amount.

**SUPPLEMENTAL SCHEDULE OF RATE COVENANT COMPLIANCE FOR FISCAL YEAR ENDED  
JUNE 30, 2014 (Legally Enacted Basis)**

(Thousands of Dollars)

LINE NO.	2014
1. Total Revenue and Beginning Fund Balance	\$ 680,455
2. Net Operating Expense	(410,797)
3. Transfer (To) From Rate Stabilization Fund	(22,925)
<b>4. Net Revenues</b>	<b>246,733</b>
5. Revenue Bonds Outstanding	(201,710)
6. General Obligation Bonds Outstanding	-
7. Pennvest Loan	-
<b>8. Total Debt Service</b>	<b>(201,710)</b>
<b>9. Net Revenue after Debt Service</b>	<b>45,023</b>
10. Transfer to General Fund	-
11. Transfer to Capital Fund	(20,194)
12. Transfer to Residual Fund	(24,829)
<b>13. Total Transfers</b>	<b>(45,023)</b>
<b>14. Net Operating Balance for Current Year</b>	<b>-</b>

The rate covenant contained in the General Ordinance requires the City to establish rates and charges for the use of the Water and Wastewater Systems sufficient to yield Net Revenues, as defined therein, in each fiscal year at least equal to 120%(coverage A) of the Debt Service Requirements for such fiscal year (excluding debt service due on any Subordinated Bonds). In addition, Net Revenues, in each fiscal year, must equal at least 100%(coverage B) of: (i) the Debt Service Requirements (including Debt Service Requirements in respect of Subordinated Bonds) payable in such fiscal year; (ii) amounts required to be deposited of Subordinated Bonds payable in such fiscal year; (ii) amounts required to be deposited into the Debt Reserve Account during such fiscal year; (iii) debt service on all General Obligations Bonds issued for the Water and Wastewater Systems payable in such fiscal year; (iv) debt service payable on Interim Debt in such fiscal year; and (v) the Capital Account Deposit Amount for such fiscal year, less amounts transferred from the Residual Fund to the Capital Account during such fiscal year. To insure compliance with the rate covenant, the General Ordinance requires that the City review its rates, rents, fees, and charges at least annually.

Additional Rate Covenant. As long as the Insured Bonds are outstanding, the City covenants to establish rates and charges for the use of the System sufficient to yield Net Revenues (excluding amounts transferred from the Rate Stabilization Fund into the Revenue Fund during, or as of the end of, such fiscal year) at least equal to 90% (coverage C) of the Debt Service Requirements (excluding debt service on any Subordinated Bonds) in such fiscal year.

COVERAGE A:	
Line 4	\$246,733
/ Line 5	\$201,710
= COVERAGE A:	1.22

COVERAGE B:	
Line 4	\$246,733
/ Line 8 + Line 11	\$221,904
= COVERAGE B:	1.11

COVERAGE C:	
Line 4 - Line 3	\$269,658
/ Line 5	\$201,710
= COVERAGE C:	1.34