



MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Financial Statements and Required
Supplementary Information

June 30, 2016

(With Independent Auditors' Report Thereon)

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

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KPMG LLP
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Independent Auditors' Report

The Board Members
Massachusetts School Building Authority:

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Massachusetts School Building Authority (the Authority), a component unit of the Commonwealth of Massachusetts, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Authority, as of June 30, 2016, and the respective changes in financial position for the year then ended in accordance with U.S. generally accepted accounting principles.



Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the management’s discussion and analysis on pages 3–9 and the schedule of funding progress and schedule of employer contributions on page 35 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management’s responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated December 14, 2016, on our consideration of the Authority’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority’s internal control over financial reporting and compliance.

KPMG LLP

Boston, Massachusetts
December 14, 2016

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Management's Discussion and Analysis – Required Supplementary Information

June 30, 2016

(Unaudited)

This section of the Massachusetts School Building Authority's (the MSBA) annual financial report presents a discussion and analysis of the MSBA's financial performance during the fiscal year ended June 30, 2016. Please read it in conjunction with the MSBA's financial statements, which follow this section.

Background

Chapter 208 of the Acts of 2004 (Chapter 208, together with Chapter 70B of the Massachusetts General Laws, Section 35BB of Chapter 10 of the Massachusetts General Laws, and Chapter 210 of the Acts of 2004, all as most recently amended, collectively referred to as the Act) eliminated the former school building assistance program and created the MSBA to administer and fund a new program (the New Program) for grants to cities, towns, and regional school districts for school construction and renovation projects.

The MSBA's major revenue source is the portion of the Commonwealth of Massachusetts (the Commonwealth)'s sales tax revenue dedicated to the MSBA. Pursuant to the Act, all monies received by the Commonwealth raised by a one percent (1%) statewide sales tax (drawn from the existing statewide 6.25% sales tax, excluding sales tax revenues on meals and from certain additional statutorily exempted revenues from sales (Dedicated Sales Tax Revenue)) are deposited into the School Modernization and Reconstruction Trust (SMART) Fund, and are available to the MSBA without further appropriation or allotment. The Dedicated Sales Tax Revenue is pledged for payment of outstanding debt service.

Under the former program, the Commonwealth was reimbursing cities, towns, and regional school districts for 728 previously approved projects (Prior Grant projects). In addition, under the former program, 428 school projects were maintained on a waiting list for funding (the Waiting List). Pursuant to the Act, the MSBA became responsible for funding the Commonwealth's share of the 728 Prior Grant projects and 428 Waiting List projects. The Commonwealth's share ranged from 50% to 90% of approved, eligible costs for each project. As of June 30, 2016, the MSBA had paid its full share of 398 of the 428 Waiting List projects and 529 of the 728 Prior Grant projects.

In fiscal year 2008, the MSBA began approving grants under the New Program for school construction and renovation projects. Under the New Program, no city, town, or regional school district or independent agricultural and technical school has any entitlement to funds from the MSBA. Grants approved by the MSBA for projects may range from 31% to 80% of approved eligible project costs. Under the New Program, the MSBA is limited by statute in the amount of grants it can approve in a fiscal year. The limit established for fiscal year 2008 was \$500 million. The limit may change annually by the lesser of 4.5% of the limit for the prior fiscal year or the percentage change in the Dedicated Sales Tax Revenue Amount (note 3) over the prior fiscal year. The aggregate grant limit for fiscal years 2008 through 2016 totals approximately \$4.5 billion.

Financial Highlights

- The government-wide net position at June 30, 2016 was a deficit of \$5.9 billion. The MSBA's government-wide net position increased by \$237 million in fiscal year 2016, primarily due to increased revenue from the SMART fund combined with reduced grant payments to municipalities for school construction and renovation projects. The reduction in grant payments results from older projects that are on hold pending final audit, combined with a number of new projects that are not requesting payment yet.

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June 30, 2016

(Unaudited)

- Total government-wide liabilities at June 30, 2016 were approximately \$7.6 billion, a decrease of \$208 million from the prior year. Total liabilities include grants payable to municipalities totaling approximately \$880 million to fund school construction and renovation projects. The grants payable liability decreased by \$200 million in fiscal year 2016 due to grant payments made to municipalities during the year and reductions of grant payment obligations due to MSBA audits and debt refundings by the local communities in which the MSBA shares in the savings based on the reimbursement rate of the project. In addition, total liabilities include \$5.6 billion of outstanding Dedicated Sales Tax Bonds and \$450 million of Commercial Paper to fund school construction and renovation projects.
- During the year, the MSBA had general revenues of \$908.9 million, comprised of \$799.4 million of sales tax revenue, \$85.5 million of investment income, and \$22.8 million of grant income as compared to general revenues of \$827.1 million in fiscal year 2015. Total revenues increased by \$81.8 million primarily due to an increase in dedicated sales tax revenue of \$32 million and an increase of \$48.3 million in investment income. The increase in investment income of \$48.3 million is primarily related to market gains in U.S. Treasuries and municipal bonds which are recorded at fair value. Fluctuations in the market value of these investments are recorded as investment income (loss). In fiscal year 2016, the change in the fair value of these investments was a \$49.6 million gain versus a gain of \$14.2 million in fiscal year 2015. The MSBA intends to hold these U.S. Treasuries and municipal bonds to maturity.
- As of June 30, 2016, the value of the grants payable liability totaled \$880.5 billion, consisting of Prior Grant projects of \$614 million, Waiting List projects of \$110.4 million, and \$156.2 million of New Program projects. The MSBA funds New Program projects on a progress payment basis. Under this process, communities submit monthly requests for reimbursement. Upon review, the MSBA processes payment for its share of eligible costs incurred. The New Program liability of \$156.2 million represents costs incurred in the New Program prior to June 30, 2016 but paid after June 30, 2016. The MSBA has approximately \$1.0 billion of commitments related to the New Program, which are not reflected in the MSBA's financial statements.
- As of June 30, 2016, the value of the outstanding Waiting List projects totaled approximately \$115.2 million, composed of the Waiting List liability of \$110.4 million and commitments of \$4.8 million. The \$4.8 million is not currently reflected in the MSBA's financial statements, but is reflected as a commitment in the notes to the financial statements (note 8).
- Total assets of the Special Revenue Fund at June 30, 2016 were \$1.43 billion compared to \$1.46 billion at June 30, 2015. Cash and cash equivalents increased by \$45.8 million due to increased unrestricted sales tax revenues and bond proceeds for grants to projects in the MSBA's capital pipeline and inherited programs. The MSBA issued \$315 million of Commercial Paper during fiscal year 2016, which will primarily be used to fund grants to cities, towns and regional school districts for school construction and renovation projects. The MSBA issued \$150 million of dedicated sales tax bonds, which will be used to fund projects in the MSBA's capital pipeline. The MSBA issued \$1.0 billion of refunding bonds during fiscal year 2016, which will primarily be used to retire longer maturity debt.
- Special Revenue Fund operations expenditures for the year ended June 30, 2016 were approximately \$15.1 million. Operations expenditures consisted of two major categories. Administrative expenditures totaling \$10.5 million consisted primarily of payroll and employee related benefits, and rent and utilities.

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June 30, 2016

(Unaudited)

Project related expenditures totaling \$4.6 million consisted primarily of expenses relating to commissioning consultants.

- The Special Revenue Fund reported a fund balance of \$1.40 billion at June 30, 2016 as compared to a fund balance of \$1.43 billion at June 30, 2015 primarily because the Amount due from the Commonwealth decreased by \$64.5 million. Cash and investments increased \$45.8 million due to the issuance of debt. Expenditures consisted of grant payments of \$626 million, debt service of \$741.6 million, operations expenditures of \$15.1 million, bond issuance costs of \$4.0 million, commercial paper repayments of \$2.5 billion, and pension expense of \$1.2 million.
- Assets of the Special Revenue Fund included cash, cash equivalents, and short-term investments of \$214.5 million; restricted cash and investments of \$979.1 million; an amount due from the Commonwealth related to the Dedicated Sales Tax Revenue totaling \$131.1 million, 100% of which was collected subsequent to year-end; loans receivable of \$99.3 million in connection with the MSBA's intergovernmental loan program for cities and towns; and, an interest receivable of \$9.0 million.
- In fiscal year 2012, the MSBA established an OPEB Trust Fund for the purposes of accumulating assets to pay for future other post-employment benefits. During fiscal year 2016, the MSBA made an additional contribution of \$100 thousand from the Special Revenue Fund to the OPEB Trust Fund. The Trust Fund remains fully funded.

Overview of the Financial Statements

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

This report consists of six financial statements presented on three pages. The first two financial statements are the Governmental Fund Balance Sheets/Statements of Net Position found on page 10. The second two financial statements are the Statements of Revenues, Expenditures and Changes in Fund Balance/Statements of Activities found on page 11. The final two financial statements are the Statements of Fiduciary Net Position and the Statements of Changes in Fiduciary Net Position found on page 12. The OPEB Trust Fund is an irrevocable trust fund established for the purpose of accumulating assets to pay for future other post-employment benefits. The assets are funded from operations and accumulate to reduce the unfunded actuarial liability of health care and other related post-employment benefits. In fiscal year 2016, the MSBA had one retiree for which benefits were incurred; thus, the direct payment of benefits is not material relative to the assets of the Trust.

Governmental Accounting Standards Board (GASB) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* requires entities to classify fund balances as restricted, committed, assigned, or unassigned. The MSBA Board of Directors has the ability to commit and un-commit funds while financial management of the MSBA has the ability to assign and un-assign funds. Restricted balances are restricted in their use by bond covenants and statute.

In accordance with GASB Statement 65: Items Previously Reported as Assets and Liabilities, losses on bond refundings are classified as deferred outflows of resources and bond issue costs are recorded as an expense when incurred.

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June 30, 2016

(Unaudited)

GASB Statement 68: *Accounting and Financial Reporting for Pensions* establishes standards for measuring and recognizing liabilities, deferred outflows of resources and deferred inflows of resources, and expense/expenditures related to pensions.

Reporting the MSBA’s Governmental Funds

The fund financial statements provide detailed information about the MSBA’s Governmental Funds – not the MSBA as a whole. The fund financial statements are prepared using a different approach than the government-wide financial statements. The MSBA’s expenditures are reported in its Governmental Funds, which focuses on cash inflows and outflows in the funds and the balance left at year-end that are available for spending. The Governmental Funds are reported using the current financial resources measurement focus and modified accrual accounting, which measures revenues as they become both measurable and available, which per MSBA policy are those amounts expected to be collected within 60 days of the end of the fiscal year. Expenditures are recorded in the period the liability is due and payable. The Governmental Fund Statements provide a detailed short-term view (less than one year) of the MSBA’s government operating requirements for the year ended June 30, 2016.

The MSBA as a Whole

The Statements of Net Position and the Statements of Activities provide information about the activities of the MSBA as a whole using the economic resources measurement focus and accrual basis of accounting, and present a longer-term view of the MSBA’s finances by focusing on total available resources and changes therein. The fund financial statements tell how operations are financed in the short term as well as what remains for future spending.

Condensed Financial Information

Summary of Net Position

(In thousands)

	<u>2016</u>	<u>2015</u>
Cash and investments	\$ 1,307,560	1,236,244
Receivables	242,929	320,695
Total assets	<u>1,550,489</u>	<u>1,556,939</u>
Deferred outflows of resources	178,697	142,805
Total assets and deferred outflows of resources	<u>1,729,186</u>	<u>1,699,744</u>
Current liabilities	1,045,103	1,062,332
Noncurrent liabilities	6,574,968	6,765,612
Total liabilities	<u>7,620,071</u>	<u>7,827,944</u>
Net position	\$ <u><u>(5,890,885)</u></u>	<u><u>(6,128,200)</u></u>

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Management’s Discussion and Analysis – Required Supplementary Information

June 30, 2016

(Unaudited)

Summary of Activities

(In thousands)

	<u>2016</u>	<u>2015</u>
Dedicated sales tax	\$ 799,359	767,361
Investment income	85,491	37,164
Grant income	22,836	22,197
Intergovernmental revenue	<u>1,214</u>	<u>393</u>
Total general revenues	<u>908,900</u>	<u>827,115</u>
Grant payments and operations	436,926	539,018
Debt service and related expenses	233,445	241,763
Pension expense	<u>1,214</u>	<u>393</u>
Total expenses	<u>671,585</u>	<u>781,174</u>
Change in net position	237,315	45,941
Net position, beginning of year	<u>(6,128,200)</u>	<u>(6,174,141)</u>
Net position, end of year	<u><u>\$ (5,890,885)</u></u>	<u><u>(6,128,200)</u></u>

These statements report the MSBA’s net position and changes to the MSBA’s net position. Annual changes in the MSBA’s net position – the difference between assets and liabilities – are one way to measure the MSBA’s health or financial position. Over time, increases or decreases in the MSBA’s net position are one indicator of whether its financial health is improving or deteriorating. The MSBA’s major revenue source is the portion of the Commonwealth’s sales tax revenue dedicated to the MSBA. Pursuant to the Act, all monies received by the Commonwealth raised by a one percent (1%) statewide sales tax (drawn from the existing statewide 6.25% sales tax, excluding sales tax revenues on meals and from certain additional statutorily exempted revenues from sales (Dedicated Sales Tax Revenue), are available to the MSBA without further appropriation or allotment. The Commonwealth has covenanted that the Dedicated Sales Tax Revenue will not be diverted from the control of the MSBA and has pledged not to reduce the sales tax rate below that prescribed by the Act. The Act states that, under the New Program, no project can be approved for funding unless the MSBA determines that the school project is within the capacity of the MSBA to finance with revenues projected to be available to the MSBA.

The MSBA reports a deficit in its net position primarily due to the fact that the MSBA has \$5.6 billion of Dedicated Sales Tax Bonds outstanding for the purposes of funding school construction and renovation projects. The MSBA also assumed responsibility for funding the Commonwealth’s share of the 428 Waiting List and 728 Prior Grant school construction and renovation projects. As of June 30, 2016, the MSBA had paid its full share of 398 of the 428 Waiting List projects and 529 of the 728 Prior Grant projects. This net position, a deficit of \$5.9 billion, will be eliminated primarily through the receipt of Dedicated Sales Tax Revenue.

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(Unaudited)

The difference between currently expendable resources reported as a fund balance in governmental funds and total available resources reported as net position in the governmental activities financial statements is identified in the adjustment columns found in the financial statements (pages 10 and 11). To arrive at the Statements of Net Position, there are adjustments for deferred outflows of resources as well as long-term and short-term liabilities that are not reported as fund assets and liabilities. Further, to arrive at the Statements of Activities, transactions relating to assets and long-term liabilities are added to or eliminated from the Statements of Revenues, Expenditures and Changes in Fund Balances. Amounts relating to the aforementioned transactions are displayed in the Adjustments column to the left of the Statements of Net Position and the Statements of Activities and in note 7 to the basic financial statements.

Debt

The Act provides the MSBA with the power to issue bonds and notes. The MSBA may issue either general obligation or special obligation bonds. Pursuant to the Act, the aggregate outstanding principal amount of the bonds shall not exceed \$10 billion. To date, the MSBA has issued a total of \$9.7 billion of Dedicated Sales Tax Bonds, including \$2.8 billion of refunding bonds, for the purpose of funding school construction and renovation projects. As of June 30, 2016, the MSBA had \$5.6 billion of Dedicated Sales Tax Bonds outstanding plus approximately \$574 million of unamortized premiums for the purpose of funding school construction and renovation projects. Coupons on the bonds range from 2.00% to 5.715% and each series is payable semiannually with the last maturity occurring in fiscal year 2046. The \$5.6 billion of debt outstanding includes \$293.4 million of Subordinated Dedicated Sales Tax Bonds. The Dedicated Sales Tax Revenue is pledged for payment of outstanding debt service on these bonds.

On July 1, 2015, the MSBA issued \$315 million of additional Commercial Paper for the funding of school construction and renovation projects. The Commercial Paper matured at various dates ranging from 33 to 97 days and interest is payable at maturity. The interest rate on this issuance of commercial paper ranges from 0.06% to 0.12%. The commercial paper that matured prior to June 30, 2016, a total of \$450 million, was rolled for maturities of 33 to 94 days at interest rates ranging from 0.41% to 0.57%.

On July 16, 2015, the MSBA retired \$300 million of Subordinated Dedicated Sales Tax Bond Anticipation Notes (2014 Series A BANs).

On December 2, 2015, the MSBA used funds on hand to defease \$35.9 million of the 2007 Dedicated Sales Tax Bonds outstanding.

On December 15, 2015, the MSBA refunded \$1.1 billion of 2007 Series A Dedicated Sales Tax Bonds by issuing \$738.4 million of Senior Sales Tax Refunding Bonds (2015 Series C Bonds) and \$291.1 million of Senior Sales Tax Refunding Bonds (2015 Series D Bonds). The Bonds mature on August 15, 2037 and the interest on the bonds is payable semi-annually on February 15th and August 15th. The interest rate on the bonds ranges from 2% to 5%. The refunding resulted in reduced debt service of \$150.3 million and a present value savings of \$108 million over the life of the debt.

On January 20, 2016, the MSBA issued \$150 million of Senior Dedicated Sales Tax Bonds (2016 Series A Bonds). The Bonds mature at various dates through November 2045 and interest is due semi-annually each May 15th and November 15th. The coupon on the bonds is 5%.

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June 30, 2016

(Unaudited)

In prior years, the MSBA defeased certain Dedicated Sales Tax Bonds by placing the proceeds of new bonds and funds on hand into irrevocable trusts with escrow agents in amounts, which will provide for payment of the principal of and interest on the defeased bonds to the redemption date. The defeased portion of such debt, accrued interest thereon, and related unamortized issuance costs and bond premiums were removed from the statements of net position. At June 30, 2016, \$1.1 billion of bonds outstanding are considered defeased.

A portion of the interest on the Dedicated Sales Tax Bonds is reimbursed by the federal government. Of the \$5.6 billion of debt outstanding as of June 30, 2016, \$450 million is taxable Build America Bonds for which the MSBA is eligible to receive a 35% interest subsidy directly from the United States Treasury. In addition, \$293 million of the Subordinated Dedicated Sales Tax Bonds, 2010 Series A Bonds and 2011 Series A Bonds, were issued as “Qualified School Construction Bonds” for which the MSBA is eligible to receive a 100% interest subsidy payment directly from the United States Treasury. During fiscal year 2013, the federal government implemented automatic budget cuts imposed through sequestration required pursuant to the Budget Control Act of 2011. Subsidy payments received from March 1, 2013 through September 30, 2013 were reduced by 8.7% due to sequestration. Subsequent notices published by the Internal Revenue Service have adjusted the sequestration rate as follows:

Date of notice	Payments affected		Sequestration rate
	From	To	
September-2013	October 1, 2013	September 30, 2014	7.20%
September-2014	October 1, 2014	September 30, 2015	7.30
August-2015	October 1, 2015	September 30, 2016	6.80
August-2016	October 1, 2016	September 30, 2017	6.90

The notice states that the sequestration reduction rate will be applied unless and until a law is enacted that cancels or otherwise impacts the sequester. Subsidy payments were reduced by approximately \$1.7 million due to sequestration in fiscal year 2016.

As of June 30, 2016, the ratings assigned to the MSBA's Dedicated Sales Tax Bonds are as follows: AA+ by Fitch Ratings, Aa2 by Moody's Investor Services, and AA+ by Standards & Poor's Investor Services. As of June 30, 2016, the ratings assigned to the MSBA's Subordinated Dedicated Sales Tax Bonds are as follows: AA by Fitch Ratings, Aa3 by Moody's Investor Services, and AA by Standards & Poor's Investor Services.

Contacting the MSBA's Financial Management

This financial report is designed to provide citizens, taxpayers, investors and creditors with a general overview of the MSBA's finances and to show the MSBA's accountability for the money it receives. If you have any questions about this report or need additional financial information, contact the Massachusetts School Building Authority at 40 Broad Street, Suite 500, Boston, MA 02109.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Governmental Fund Balance Sheet/Statement of Net Position

June 30, 2016

(Dollars in thousands)

Assets	Special Revenue Fund	Debt Service Fund	Adjustments (note 7)	Statement of net position
Current assets:				
Cash, cash equivalents, and short-term investments (note 4)	\$ 214,519	—	—	214,519
Restricted cash and investments (note 4)	979,119	113,922	—	1,093,041
Amount due from Commonwealth (note 3)	131,051	—	—	131,051
Interest receivable	8,995	—	—	8,995
Grant receivable	—	—	3,489	3,489
Loan receivable (note 9)	6,437	—	—	6,437
Noncurrent assets:				
Loan receivable (note 9)	92,841	—	—	92,841
Other assets	—	—	116	116
Total assets	1,432,962	113,922	3,605	1,550,489
Deferred outflows of resources:				
Loss on bond refunding	—	—	178,697	178,697
Total assets and deferred outflows	\$ 1,432,962	113,922	182,302	1,729,186
Liabilities				
Current liabilities:				
Accounts payable	\$ 1,824	—	—	1,824
Accrued interest	—	—	86,524	86,524
Current portion of grants payable (notes 5 and 6)	30,761	—	316,245	347,006
Current portion of long-term debt (note 5)	—	—	112,925	112,925
Current portion of compensated absences (note 5)	—	—	272	272
Commercial paper (note 5)	—	—	450,000	450,000
Current portion of bond premium (notes 5 and 7)	—	—	46,552	46,552
Long-term liabilities:				
Long-term debt (note 5)	—	—	5,511,350	5,511,350
Grants payable (notes 5 and 6)	—	—	533,531	533,531
Bond premium (notes 5 and 7)	—	—	527,704	527,704
Compensated absences (note 5)	—	—	196	196
Arbitrage rebate (note 5)	—	—	2,187	2,187
Total liabilities	32,585	—	7,587,486	7,620,071
Fund balance/net position:				
Restricted for debt service	979,119	113,922	(1,093,041)	—
Assigned	421,258	—	(421,258)	—
Total fund balance	1,400,377	113,922	(1,514,299)	—
Total liabilities and fund balance	\$ 1,432,962	113,922		
Restricted for debt service				1,093,041
Unrestricted				(6,983,926)
Commitments and contingencies (notes 8 and 10)				
Net position				\$ (5,890,885)

See accompanying notes to financial statements.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Statement of Revenues, Expenditures, and Changes in Fund Balance/Statement of Activities

Year ended June 30, 2016

(Dollars in thousands)

	<u>Special Revenue Fund</u>	<u>Debt Service Fund</u>	<u>Adjustments (note 7)</u>	<u>Statement of activities</u>
General revenues:				
Dedicated sales tax (note 3)	\$ 799,359	—	—	799,359
Investment income	75,158	10,760	(427)	85,491
Grant income	25,770	—	(2,934)	22,836
Intergovernmental revenue	1,214	—	—	1,214
Total revenues	<u>901,501</u>	<u>10,760</u>	<u>(3,361)</u>	<u>908,900</u>
Expenditures/expenses:				
Grant payments (note 6)	626,000	—	(204,039)	421,961
Operations	15,141	—	(176)	14,965
Bond issuance costs	4,048	—	—	4,048
Loss on refunding	—	—	10,872	10,872
Debt service	741,642	—	(523,117)	218,525
Commercial paper repayments	2,519,000	—	(2,519,000)	—
Pension expense	1,214	—	—	1,214
Total expenditures/expenses	<u>3,907,045</u>	<u>—</u>	<u>(3,235,460)</u>	<u>671,585</u>
Other financing sources (uses):				
Arbitrage Rebate Payment (note 5)	(11,842)	—	11,842	—
Bond proceeds (note 5)	1,209,977	—	(1,209,977)	—
Commercial paper proceeds	2,834,000	—	(2,834,000)	—
Payments to Escrow Agent	(1,189,246)	—	1,189,246	—
Bond Premium	144,709	—	(144,709)	—
Transfer to (from) funds	(14,745)	14,745	—	—
Total other financing sources (uses)	<u>2,972,853</u>	<u>14,745</u>	<u>(2,987,598)</u>	<u>—</u>
Change in fund balance/net position	(32,691)	25,505	244,501	237,315
Fund balance/net position, beginning of year	1,433,068	88,417	(7,649,685)	(6,128,200)
Fund balance/net position, end of year	<u>\$ 1,400,377</u>	<u>113,922</u>	<u>(7,405,184)</u>	<u>(5,890,885)</u>

See accompanying notes to financial statements.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Fiduciary Fund

June 30, 2016

(Dollars in thousands)

Statement of Fiduciary Net Position

	OPEB Trust Fund
Assets:	
Cash, cash equivalents, and short-term investments (note 4)	\$ <u>2,670</u>
Total assets	<u>2,670</u>
Net position – held in trust for OPEB benefits	\$ <u><u>2,670</u></u>

Statement of Changes in Fiduciary Net Position

Additions:	
Contributions:	
Employer	\$ <u>100</u>
Total contributions	<u>100</u>
Net investment income:	
Net appreciation (depreciation)	(4)
Interest income	70
Total investment expense	<u>(14)</u>
Net investment income	<u>52</u>
Total additions	152
Net position, beginning of period	<u>2,518</u>
Net position, end of period	\$ <u><u>2,670</u></u>

See accompanying notes to financial statements.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(1) Organization and Background

Chapter 208 of the Acts of 2004 (Chapter 208, together with Chapter 70B of the Massachusetts General Laws, Section 35BB of Chapter 10 of the Massachusetts General Laws and Chapter 210 of the Acts of 2004, all as most recently amended, collectively referred to as the Act), eliminated the former school building assistance program and created the Massachusetts School Building Authority (the MSBA) to administer and fund a new program (the New Program) for grants to cities, towns, and regional school districts for school construction and renovation projects.

Under the former program, the Commonwealth of Massachusetts (the Commonwealth) was reimbursing cities, towns, and regional school districts for its share of 728 previously approved projects (Prior Grant Projects). In addition, under the former program, 428 school projects were maintained on a waiting list for funding (the Waiting List). Pursuant to the Act, the MSBA became responsible for funding the Commonwealth's share of the 728 Prior Grant projects and 428 Waiting List projects. The Commonwealth's share ranged from 50% to 90% of approved eligible costs. As of June 30, 2016, the MSBA had paid in full its share of 398 of the 428 Waiting List projects and 529 of the 728 Prior Grant projects.

Under the New Program, no city, town, regional school district, or independent agricultural and technical school has any entitlement to funds from the MSBA. Grants approved by the MSBA for projects may range from 31% to 80% of approved eligible project costs. Under the New Program, the MSBA is limited in the amount of grants it can approve in a fiscal year. The limit may change by the lesser of 4.5% of the limit for the prior fiscal year or the percentage change in the Dedicated Sales Tax Revenue Amount (note 3) over the prior fiscal year.

The MSBA is mandated with achieving the effective planning, management, and financial sustainability of a school building assistance program. The MSBA is an independent public Authority not subject to the supervision and control of any other executive office, department, agency, or political subdivision of the Commonwealth. The MSBA is funded by a dedicated portion of the Commonwealth's statewide sales tax revenue. The Commonwealth has covenanted that the Dedicated Sales Tax Revenue will not be diverted from the control of the MSBA and has pledged not to reduce the sales tax rate below that prescribed by the Act. The Act prohibits the MSBA from filing for bankruptcy. The Act provides the MSBA with the power to issue bonds and notes. The MSBA may issue either general obligation or special obligation bonds. Pursuant to the Act, the aggregate outstanding principal amount of the bonds shall not exceed \$10 billion.

Under the Act, the MSBA Board shall consist of the Treasurer and Receiver General of the Commonwealth (the Treasurer), the Secretary of Administration and Finance, and the Commissioner of Education, each *ex officio*, or such persons' designees, and four other members appointed by the Treasurer, each of whom shall serve two year terms and shall be eligible for reappointment. Of the four members appointed by the Treasurer, two are required to have practical experience in educational facilities planning, school building construction, or architecture and school design, and two are required to be persons in the field of education with demonstrated knowledge of the Commonwealth's curriculum frameworks and other relevant federal and state educational standards. The Treasurer serves as the chairperson of the MSBA. The Executive Director of the MSBA serves as Secretary of the MSBA Board, *ex officio*.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(2) Summary of Significant Accounting Policies

(a) *Reporting Entity and Basis of Presentation*

The accompanying financial statements of the MSBA have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). The MSBA has prepared government-wide financial statements titled "Statements of Net Position" and "Statements of Activities". The MSBA also prepares the fund financial statements, which are the Special Revenue Fund and Debt Service Fund "Balance Sheets" and "Statements of Revenues, Expenditures and Changes in Fund Balance." The MSBA's basic financial statements include both the government-wide and the fund financial statements.

Governmental Fund Financial Statements – The MSBA utilizes the current resources measurement focus and modified accrual basis of accounting in the preparation of the governmental fund financial statements. Revenues and related receivables are recognized when they become both measurable and available. "Available" means collectible within the current period or soon enough thereafter to pay liabilities of the current period, which is 60 days after year end. Expenditures and related liabilities are generally recorded in the period in which the liability is incurred. However, expenditures related to debt service, compensated absences, and grants payable are recorded only to the extent that the liabilities mature (come due for payment).

Operating expenditures are direct costs incurred by the MSBA and are categorized into administrative expenditures, such as payroll related benefits and legal fees, and project related expenditures, such as professional consultants and other related costs.

Other financing sources (uses) primarily relate to the issuance of long-term debt.

The MSBA reports the following funds:

The Special Revenue Fund is the MSBA's primary operating fund. It accounts for all financial resources of the MSBA, except those required to be accounted for in another fund.

The Debt Service Fund is a sinking fund related to the 2010 Series A Bonds and 2011 Series A Bonds. The amounts in the Debt Service Fund will be used to pay the principal of the 2010 Series A Bonds and 2011 Series A Bonds at maturity. Periodically, money is transferred from the Special Revenue Fund to the Debt Service Fund to meet sinking fund requirements. During fiscal year 2016, there was a transfer of \$14.7 million from the Special Revenue Fund to the Debt Service Fund. As of June 30, 2016, the fund balance in the Debt Service Fund totaled \$113.9 million.

Fiduciary Fund – During fiscal year 2012, the MSBA established the OPEB Trust Fund, an irrevocable trust fund established to accumulate assets for the purpose of paying for future other post-employment benefits. The assets are funded from operations and accumulate to reduce the unfunded actuarial liability of health care and other related post-employment benefits. In fiscal year 2016, the MSBA had one retiree for which benefits were incurred and were paid from the special revenue fund; thus, the direct payment of benefits is not material relative to the assets of the Trust benefits. The Trust Fund financial statements utilize the economic resources measurement focus and the accrual basis of accounting.

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June 30, 2016

Government-wide Financial Statements – The MSBA utilizes the economic resources measurement focus and the accrual basis of accounting, in the preparation of the government-wide financial statements. Accordingly, changes in long-term assets and liabilities are incorporated into these financial statements. Since the governmental fund financial statements are prepared on a different measurement focus and basis of accounting than the government-wide financial statements, an “Adjustments Column” is presented to convert the fund basis financial statements into the government-wide financial statements. Details supporting amounts in the Adjustments Column are presented in note 7.

Due to its relationship with the Commonwealth, the MSBA is considered a blended component unit for financial statement purposes and is presented as a governmental fund in the Commonwealth’s financial statements. The MSBA has no relationship with other entities that could be considered component units.

(b) Investments

The MSBA has investments in U.S. Treasuries, municipal bonds, money markets, an external investment pool, and a Guaranteed Investment Contract.

The MSBA invests in the Massachusetts Municipal Depository Trust (MMDT), which is an external investment pool that is overseen by the Massachusetts State Treasurer and is not SEC registered. The investment in MMDT is valued at amortized cost. MMDT has no redemption restrictions.

Fluctuations in the fair value of U.S. Treasuries and municipal bonds are recorded as investment income (loss). Investment income (loss) related to fluctuations in value of these investments was \$49.6 million in fiscal year 2016. The MSBA intends to hold these investments to maturity.

The MSBA has implemented GASB Statement No. 72, *Fair Value Measurement and Application*. This statement requires that certain assets, primarily investments, be recorded at fair value, as well as establishes a three-level hierarchy for fair value measurements based on the nature of inputs used in the valuation of an asset or liability as of the reporting date.

(c) Capital Assets

Capital assets are defined by the MSBA as classes of assets with an initial aggregate cost of more than \$100,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed.

Leasehold improvements exceeding \$100,000 are capitalized and amortized over the life of the lease which is ten years. The book value of capitalized leasehold improvements associated with the MSBA’s lease totals \$116,000 as of June 30, 2016.

(d) Compensated Absences

Employees earn the right to be compensated during absences for vacation and illness. Vested or accumulated vacation and sick leave expected to be liquidated with expendable available financial resources are reported as expenditures and liabilities. Employees are granted vacation and sick leave in varying amounts based on years of service. Upon retirement, termination, or death, certain

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employees are compensated for unused vacation and sick leave (subject to certain limitations) at their then-current rate of pay. At June 30, 2016, approximately \$468 thousand of accrued compensated absences has been recorded in the government-wide financial statements.

(e) *Deferred Inflows of Resources and Deferred Outflows of Resources*

The MSBA accounts for certain transactions that represent inflows and outflows of resources during one period that are applicable to future periods as deferred outflows of resources and deferred inflows of resources, respectively, to distinguish them from assets and liabilities. For fiscal 2016, the MSBA has reported deferred outflows pertaining to the deferred losses on its debt refunding transactions.

(f) *Revenue Recognition*

The MSBA’s major revenue source is the portion of the Commonwealth’s sales tax revenue dedicated to the MSBA. Pursuant to the Act, all monies received by the Commonwealth raised by a one percent (1%) statewide sales tax (drawn from the existing statewide 6.25% sales tax, excluding sales tax revenues on meals and from certain additional statutorily exempted revenues from sales (Dedicated Sales Tax Revenue)) are deposited into the School Modernization and Reconstruction Trust (SMART) Fund, and are available to the MSBA without further appropriation or allotment. The use of the SMART Fund is exclusively restricted for the purposes of the MSBA. Revenue is recognized and a corresponding “Amount due from Commonwealth” is recorded to reflect revenue earned in period of underlying sale. The Dedicated Sales Tax Revenue is pledged for repayment of outstanding debt service.

100% of the interest on the \$293.4 million of Subordinated Dedicated Sales Tax Bonds and 35% of the interest on the \$450.0 million of Build America Bonds is eligible to be reimbursed by the federal government and recorded as grant income. Beginning in fiscal 2013 and continuing through fiscal 2016, the federal government implemented automatic budget cuts imposed through sequestration required pursuant to the Budget Control Act of 2011. Subsidy payments received from March 1, 2013 through September 30, 2013 were reduced by 8.7% (5.1% on an annualized basis) due to sequestration. Subsequent notices published by the Internal Revenue Service have adjusted the sequestration rate as follows:

<u>Date of notice</u>	<u>Payments affected</u>		<u>Sequestration rate</u>
	<u>From</u>	<u>To</u>	
September-2013	October 1, 2013	September 30, 2014	7.20%
September-2014	October 1, 2014	September 30, 2015	7.30
August-2015	October 1, 2015	September 30, 2016	6.80
August-2016	October 1, 2016	September 30, 2017	6.90

The notice states that the sequestration reduction rate will be applied unless and until a law is enacted that cancels or otherwise impacts the sequester. Subsidy payments were reduced by approximately \$1.7 million due to sequestration during fiscal year 2016.

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(g) **Grants Payable**

The MSBA records a liability for its share of total eligible project costs differently depending on the type of project. However, for all projects, the MSBA recognizes a liability for its estimated share of total eligible project costs when the applicable eligibility requirements have been met.

Prior Grants – All of the 728 Prior Grant projects had been receiving an annual payment under the former program. The liability for these projects will be reduced over time through annual payments, and savings from debt refundings by the local communities in which the MSBA shares in the savings based on the reimbursement rate of the project. These projects operate similar to Prior Grant projects.

Waiting List – The MSBA funds Waiting List projects using two different methods, lump sum and progress payments. Each funding method has different eligibility requirements.

Waiting List projects that are under the lump sum method were recognized as a liability once construction started. The liability for these projects will be reduced over time through annual payments and savings from debt refundings by the local communities in which the MSBA shares in the savings based on the reimbursement rate of the project. These projects operate similar to Prior Grant projects.

Under the progress payment method, the MSBA's share of costs incurred are generally recognized as a liability once a grantee requests reimbursement from the MSBA. Of the \$110.4 million liability associated with Waiting List projects, the liability related to the progress payment method is approximately \$4 million.

Waiting List projects that are not currently recognized as a liability are considered commitments of the MSBA. As of June 30, 2016, the amount of commitments outstanding for the Waiting List projects is \$4.8 million, and is anticipated to be funded under the progress payment method.

New Program – The MSBA funds New Program projects on a progress payment basis. Under this process, communities may submit reimbursement requests no more frequently than once per month. Upon review, audit, and approval, the MSBA processes payment for its share of eligible costs incurred. The MSBA's share of costs incurred for New Program projects are recognized as a liability once a grantee's request for reimbursement is reviewed, audited, and approved by the MSBA. The MSBA has recorded a liability of \$29.1 million in the special revenue fund for reimbursements received, reviewed, and approved for payment by June 30, 2016. Additionally, a long term liability of \$127 million was recorded for the reimbursements not reviewed or approved for payment prior to June 30, 2016, as well as final project hold back payments subject to final audit and Board approval after year end. New Program projects that are not currently recognized as a liability are considered commitments of the MSBA. As of June 30, 2016, the amount of commitments outstanding for the New Program projects is \$1.0 billion, and will be funded under the progress payment method.

For all projects, regardless of the funding mechanism, costs incurred by the grantees are subject to audit by the MSBA. Completion of these audits will allow the MSBA to determine the final approved cost of these projects, and the MSBA will adjust the payments it makes for these projects, as necessary, in accordance with the results of those audits.

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Notes to Financial Statements

June 30, 2016

(h) *Employee Benefits*

The Commonwealth is responsible by statute for the pension benefits for members of the State Employees' Retirement System (SERS), including employees of the MSBA. The SERS is a cost-sharing, multi-employer public employee retirement system, covering substantially all employees of the Commonwealth and certain employees of independent authorities and agencies. The SERS is administered by the Commonwealth and is part of its reporting entity; no stand-alone financial report is issued. MSBA is not required to make employer contributions to SERS.

The MSBA provides employment benefits other than pensions, including health care and life insurance benefits for active and retired employees through participation in the Commonwealth's Group Insurance Commission. MSBA employees may become eligible for post-employment benefits if they reach normal retirement age while working for the MSBA and retire from the MSBA. The MSBA records other post-employment benefits (OPEB) as expenses when earned by the employee. The MSBA currently funds OPEB based on an actuarial funding schedule, which was fully funded as of June 30, 2016. As of June 30, 2016, the MSBA had three retirees.

(i) *Use of Estimates*

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

(j) *Fund Balances*

GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* requires entities to classify fund balances as restricted, committed, assigned, or unassigned. The MSBA Board of Directors has the ability to commit and un-commit funds while financial management of the MSBA has the ability to assign and un-assign funds. Restricted balances are restricted in their use by bond covenants or statute.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

As of June 30, 2016, the MSBA had the following fund balances (in thousands):

	Amount
Fund balance:	
Restricted:	
Debt service*	\$ 1,093,041
Subtotal	1,093,041
Assigned:	
Arbitrage rebate	2,187
Grants and loans to cities, towns, and regional school districts	419,071
Subtotal	421,258
Total fund balance	\$ 1,514,299

* \$113.9 million relates to the debt service fund

(3) Amount due from Commonwealth

Coincident with the establishment of the MSBA, the Commonwealth established the SMART Fund for the purpose of receiving the transfer of Dedicated Sales Tax Revenue and other funds from the Commonwealth to the MSBA. Amounts held in this Fund are for the exclusive purpose of the MSBA. In fiscal year 2016, \$799.4 million of Dedicated Sales Tax Revenue was earned and recorded as revenue. Of that amount, \$131.1 million was received subsequent to year-end and is recorded as a receivable on the MSBA's financial statements. The Dedicated Sales Tax Revenue is pledged for repayment of outstanding debt service.

(4) Deposits and Investments

GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, requires that entities disclose essential risk information about deposits and investments.

(a) Investment Policy

Pursuant to the Act, the MSBA is authorized to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, bonds, or notes of public agencies or municipalities, bank time deposits, guaranteed investment contracts, money market accounts, and repurchase agreements. The MSBA has an investment policy that establishes minimum credit quality for certain instruments, outlines investment procedures, and provides for periodic reporting. The MSBA's investment policy does not specifically limit the amount the MSBA may invest in any one issuer.

The assets of the MSBA's OPEB Trust Fund are invested in the State Retiree Benefits Trust Fund, which is managed by the Massachusetts Pension Reserves Investment Trust Fund and follows the investment policy of the Massachusetts Pension Reserves Investment Management Board.

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Notes to Financial Statements

June 30, 2016

(b) Custodial Credit Risk

Custodial credit risk is the risk that in the event of bank failure, the MSBA's deposits may not be returned. The MSBA does not have a formal investment policy for custodial credit risk. As of June 30, 2016, the bank balances of uninsured and uncollateralized deposits totaled \$55,944.

(c) Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of the MSBA's investments. The MSBA's investment policy does not specifically limit investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. The MSBA intends to hold its fixed income investments to maturity.

The following is a list of the MSBA's investments and related maturity schedule as of June 30, 2016 (dollars in thousands):

<u>Investment type</u>	<u>Fair value</u>	<u>Investment maturities</u>			
		<u>< 1 Year</u>	<u>1-5 Years</u>	<u>6-10 Years</u>	<u>>10 Years</u>
Money Market Funds	\$ 195,981	195,981	—	—	—
External investment pool	2,749	2,749	—	—	—
U.S. Treasuries	444,509	—	18,437	—	426,072
Municipal Bonds	83,750	—	—	—	83,750
GIC	200,098	—	—	—	200,098
Total	\$ <u>927,087</u>	<u>198,730</u>	<u>18,437</u>	<u>—</u>	<u>709,920</u>

(d) Credit Risk

As of June 30, 2016, the MSBA had \$200.1 million invested in a GIC for which collateral equal to 105% of the principal value of the contract is held by a third party. This investment is not rated.

As of June 30, 2016 the MSBA had \$444.5 million invested in Treasury STRIPS and other U.S. obligations backed by the full faith and credit of the U.S. government.

As of June 30, 2016, the MSBA had \$196.0 million invested in institutional money market funds valued at fair value. These investments were rated AAA.

As of June 30, 2016, the MSBA had \$83.8 million invested in municipal bonds. These investments were rated AA+ or above.

As of June 30, 2016, the MSBA had \$2.7 million invested in MMDT. This investment was not rated.

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Notes to Financial Statements

June 30, 2016

(e) **Concentration of Credit Risk – Investments**

Concentration of credit risk is the risk of loss attributed to the magnitude of a government’s investment in a single issuer. The issuers where investments as of June 30, 2016 exceeded 5% of the MSBA’s total investments, other than investments in U.S. government obligations and money market funds, are as follows:

	Percentage of total investments
GIC FSA Capital Management Services, LLC	22%
MA Transit	6

(f) **Fair Value Measurements**

The MSBA categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

The following is a description of the valuation methodologies used for assets measured at fair value. There have been no changes in the methodologies used at June 30, 2016.

U.S. Treasury Securities - Securities issued by the U.S. government, its agencies, authorities, and instrumentalities are valued using quoted prices and a pricing model maximizing the use of observable inputs determined by investment managers. U.S. Treasury Securities consist principally of U.S. Treasury bills, notes, and bonds, which are generally classified as Level 1 of the fair value hierarchy

SLGS - consist of securities issued under the State and Local Government Series (SLGS) securities program. The securities consist principally of certificates of indebtedness, notes, or bonds with maturities from 15 days to 40 years. SLGS are generally valued using a pricing model maximizing the use of observable inputs determined by investment managers. SLGS are generally classified as Level 2 of the fair value hierarchy

Municipal securities - State and municipal securities are generally valued based on the independent prices obtained from third party evaluated services. Where prices of recently executed market transactions of similar securities of comparable size are easily observed, those are taken into consideration for arriving at the fair value. When independent prices are available for state and municipal bonds, these are categorized as Level 2 of the fair value hierarchy.

The MSBA has the following recurring fair value measurements as of June 30, 2016:

U.S. Treasury securities of \$435.7 million are valued using quoted market prices (Level 1 inputs).

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Notes to Financial Statements

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Institutional money market funds of \$196 million are valued at \$1.00 per share, which approximates fair value of the investment (Level 1 inputs).

State and Local Government Series Securities (SLGS) of \$8.8 million are valued using inputs other than quoted prices (Level 2 inputs).

Municipal securities of \$83.8 million are valued using inputs other than quoted prices (Level 2 inputs).

(5) Long and Short-Term Obligations

Following is a summary of the long-term obligations of the MSBA as of June 30, 2016 (amounts in thousands):

	Outstanding, beginning of year	Additions	Reductions*	Outstanding, end of year	Due within one year
Grants payable:					
Prior Grant projects	\$ 802,215	—	188,258	613,957	170,775
Waiting List projects	126,131	11,642	27,354	110,419	20,070
New Program projects	152,673	417,198	413,710	156,161	156,161
	<u>1,081,019</u>	<u>428,840</u>	<u>629,322</u>	<u>880,537</u>	<u>347,006</u>
Long-term debt:					
Dedicated Sales Tax Bonds (2007)	1,373,380	—	1,157,380	216,000	—
Dedicated Sales Tax Bonds (2009A)	29,900	—	3,900	26,000	9,000
Dedicated Sales Tax Bonds (2009B) – Build America Bonds	450,000	—	—	450,000	—
Subordinated Dedicated Sales Tax Bonds (2010A) – Qualified School Construction Bonds	151,000	—	—	151,000	—
Subordinated Dedicated Sales Tax Bonds (2011A) – Qualified School Construction Bonds	142,380	—	—	142,380	—
Dedicated Sales Tax Bonds (2011B)	959,755	—	19,000	940,755	27,885
Dedicated Sales Tax Bonds (2012A)	766,140	—	—	766,140	—

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	Outstanding, beginning of year	Additions	Reductions*	Outstanding, end of year	Due within one year
Dedicated Sales Tax Bonds (2012B)	\$ 916,350	—	—	916,350	—
Dedicated Sales Tax Bonds (2013A)	549,000	—	4,510	544,490	—
Dedicated Sales Tax Bonds (2015A)	76,315	—	76,315	—	—
Dedicated Sales Tax Bonds (2015B)	300,190	—	8,510	291,680	13,125
Dedicated Sales Tax Bonds (2015C)	—	738,405	—	738,405	60,705
Dedicated Sales Tax Bonds (2015D)	—	291,075	—	291,075	—
Dedicated Sales Tax Bonds (2016A)	—	150,000	—	150,000	2,210
	<u>5,714,410</u>	<u>1,179,480</u>	<u>1,269,615</u>	<u>5,624,275</u>	<u>112,925</u>
Other liabilities:					
Compensated absences	527	132	191	468	272
Bond Anticipation Notes	300,000	—	300,000	—	—
Commercial paper	135,000	2,834,000	2,519,000	450,000	450,000
Arbitrage rebate	13,603	426	11,842	2,187	—
	<u>449,130</u>	<u>2,834,558</u>	<u>2,831,033</u>	<u>452,655</u>	<u>450,272</u>
Total long-term obligations	\$ <u>7,244,559</u>	<u>4,442,878</u>	<u>4,729,970</u>	<u>6,957,467</u>	<u>910,203</u>

* Includes reductions in grants payable due to MSBA audits and debt refundings by the local communities of \$3.8 million for Prior Grant projects.

Maturity of Bond Indebtedness

Bond indebtedness outstanding at June 30, 2016 matures as follows (amounts in thousands):

	Principal	Interest	Interest subsidy	Total
Year ending June 30:				
2017	\$ 112,925	275,381	(22,550)	365,756
2018	118,665	269,635	(23,663)	364,637
2019	149,245	263,992	(24,213)	389,024
2020	140,335	256,478	(24,213)	372,600
2021	147,235	249,582	(24,213)	372,604
2022–2026	785,455	1,133,614	(121,065)	1,798,004
2027–2031	1,405,090	873,027	(70,650)	2,207,467
2032–2036	1,182,595	550,357	(33,780)	1,699,172
2037–2041	1,143,235	229,260	(8,950)	1,363,545
2042–2046	439,495	33,290	—	472,785
	<u>\$ 5,624,275</u>	<u>4,134,616</u>	<u>(353,297)</u>	<u>9,405,594</u>

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Notes to Financial Statements

June 30, 2016

As of June 30, 2016, the MSBA had outstanding approximately \$5.6 billion of Dedicated Sales Tax bonds, plus approximately \$574.3 million of unamortized premiums, for the purpose of funding school construction and renovation projects. Coupons on the bonds range from 2.000% to 5.715%, and each series is payable semi-annually with the last maturity occurring in fiscal year 2046. The \$5.6 billion of debt outstanding includes \$293.4 million of Subordinated Dedicated Sales Tax Bonds.

On July 1, 2015, the MSBA issued \$315 million of additional Commercial Paper for the funding of school construction and renovation projects. The Commercial Paper matured at various dates ranging from 33 to 97 days with interest payable at maturity. The interest rate on this issuance of commercial paper ranged from 0.06% to 0.12%. The commercial paper that matured prior to June 30, 2016, a total of \$450 million, was rolled for maturities of 33 to 94 days at interest rates ranging from 0.41% to 0.57%.

On July 16, 2015, the MSBA retired \$300 million of Subordinated Dedicated Sales Tax Bond Anticipation Notes (2014 Series A BANs).

On December 2, 2015, the MSBA used funds on hand to defease \$35.9 million of the 2007 Series A Dedicated Sales Tax Bonds outstanding.

On December 15, 2015, the MSBA refunded \$1.1 billion of 2007 Series A Dedicated Sales Tax Bonds by issuing \$738.4 million of Senior Sales Tax Refunding Bonds (2015 Series C Bonds) and \$291.1 million of Senior Sales Tax Refunding Bonds (2015 Series D Bonds). The Bonds mature on August 15, 2037 and the interest on the bonds is payable semi-annually on February 15th and August 15th. The interest rate on the bonds ranges from 2.0% to 5%. The refunding resulted in reduced debt service of \$150.3 million and a present value savings of \$108 million over the life of the debt.

On January 20, 2016, the MSBA issued \$150 million of Senior Dedicated Sales Tax Bonds (2016 Series A Bonds). The Bonds mature at various dates through November 2045 and interest is due semi-annually each May 15th and November 15th. The coupon on the bonds is 5%.

The MSBA has defeased certain Dedicated Sales Tax Bonds by placing the proceeds of new bonds and funds on hand into irrevocable trusts with escrow agents in amounts which will provide for payment of the principal and interest on the defeased bonds to the redemption date. The defeased portion of such debt, accrued interest thereon, and related unamortized issuance costs and bond premiums were removed from the statements of net position. At June 30, 2016, \$1.1 billion of bonds outstanding are considered defeased.

A portion of the interest on the Dedicated Sales Tax Bonds is reimbursed by the federal government. Of the \$5.6 billion of debt outstanding as of June 30, 2016, \$450 million is taxable Build America Bonds for which the MSBA is eligible to receive a 35% interest subsidy directly from the United States Treasury. In addition, \$293.4 million of the Subordinated Dedicated Sales Tax Bonds were issued as "Qualified School Construction Bonds" for which the MSBA is eligible to receive a 100% interest subsidy payment directly from the United States Treasury. During fiscal year 2013, the federal government implemented automatic budget cuts imposed through sequestration required pursuant to the Budget Control Act of 2011. Subsidy payments received from March 1, 2013 through September 30, 2013 were reduced by 8.7% (5.1% on an annualized basis) due to sequestration. In August, 2015, the IRS published a notice indicating that subsidy payments processed on or after October 1, 2015 and on or before September 30, 2016 will be reduced by the fiscal year 2016 sequestration rate of 6.8%. The notice states that the sequestration reduction rate will

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

be applied unless and until a law is enacted that cancels or otherwise impacts the sequester. Subsidy payments were reduced by approximately \$1.7 million due to sequestration in fiscal year 2016.

Credit Facilities

During FY16, the MSBA maintained credit facilities to provide liquidity support for commercial paper notes totaling \$450 million. The \$150 million Commercial Paper Notes, Series 2015 A, are secured by an irrevocable letter of credit (“LOC”) provided by Bank of America, N.A., which expires in March 2018. The \$150 million Commercial Paper Notes, Series 2015 B, are secured by an irrevocable letter of credit (“LOC”) provided by Citibank, N.A., which expires in March 2018. The \$150 million Commercial Paper Notes, Series 2015 C, are secured by an irrevocable letter of credit (“LOC”) provided by Barclays Bank PLC, which expires in March 2018. As of June 30, 2016, there were no draws against available balances on the three lines of credit.

(6) Grants Payable

As of June 30, 2016, the liability for future payments related to the Prior Grant and Waiting List projects is as follows (amounts in thousands):

	<u>Prior Grants</u>	<u>Waiting List</u>	<u>Total</u>
Year ending June 30:			
2017	\$ 170,775	20,070	190,845
2018	138,574	15,299	153,873
2019	122,856	15,299	138,155
2020	91,115	15,299	106,414
2021	58,751	15,299	74,050
2022–2025	31,886	29,153	61,039
Total	\$ <u>613,957</u>	<u>110,419</u>	<u>724,376</u>

The amounts to be reimbursed for the Prior Grant and Waiting List projects may decrease as a result of debt refundings by the local communities in which the MSBA shares in the savings based on the reimbursement rate of the project.

The MSBA will also fund its share of eligible project costs for Waiting List projects and New Program projects that are not currently recognized as a liability. The MSBA has estimated the amount of outstanding Waiting List commitments and New Program commitments at June 30, 2016 to be approximately \$4.8 million and \$1.0 billion, respectively.

Upon completion of the projects, all costs incurred by the grantees are subject to audit by the MSBA and, based on the results of the audits, the estimated approved eligible costs and the related liability may either increase or decrease.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(7) Adjustments Column

(a) *Explanation of Certain Differences between the Governmental Fund Balance Sheets and the Statements of Net Position*

Long-term liabilities of the MSBA's activities are not due and payable in the current period and, therefore, are not reported as fund liabilities. Also, some assets used in governmental activities are not financial resources and, therefore, are not reported as fund assets. All assets and liabilities, both current and long-term, are reported in the statements of net position. The difference between the governmental fund balances and governmental activities net position at June 30, 2016 were as follows (amounts in thousands):

Total fund balance – governmental funds	\$	1,514,299
Amounts reported for governmental activities in the statement of net position are different because:		
Grants receivable is capitalized in the government-wide statements		3,489
Other assets are capitalized in the government-wide statements		116
Loss on bond refundings is classified as deferred outflows of resources in the government-wide statements		178,697
Some liabilities are not due and payable in the current period and, therefore, are not reported in the governmental funds.		
Those liabilities consist of:		
Dedicated sales tax bonds		(5,624,275)
Grants payable to local communities		(849,776)
Bond premiums		(574,256)
Commercial paper		(450,000)
Accrued interest		(86,524)
Arbitrage rebate		(2,187)
Compensated absences		(468)
Net position of governmental activities	\$	(5,890,885)

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(b) *Explanation of Certain Differences between the Governmental Fund Statements of Revenues, Expenditures, and Changes in Fund Balance and the Statements of Activities*

In the statements of activities all revenues and expenses are recognized in the year they are earned or incurred, regardless of when they are paid. In the governmental funds, payments and receipts contribute to the change in fund balance, while the same payments and receipts decrease and increase liabilities in the statements of net position. These differences in measurement and recognition affect both the reported fund balance and the reported net position. Adjustments required to be made to the reported governmental funds to arrive at the statements of activities are as follows (amounts in thousands):

Net change in fund balances – governmental funds	\$	(7,185)
Amounts reported for governmental activities in the statement of activities are different because:		
Payments and adjustments on grants decrease long-term liabilities in the statement of net position, but are included as expenditures in the governmental funds.		204,039
Some expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds. This amount represents the change in compensated absences, interest payable, and arbitrage rebate		1,145
Proceeds of long-term debt and premiums increase long-term liabilities in the statement of net position but, are included in the operating statement of the governmental funds.		(4,188,686)
Repayment of bond principal and payments to escrow agents are expenditures in the governmental funds, but reduce long-term liabilities on the statement of net position.		4,231,363
Adjustment of revenues reported in the statement of activities on a different basis than in the governmental funds.		<u>(3,361)</u>
Change in net position of governmental activities	\$	<u><u>237,315</u></u>

(8) Commitments and Contingencies

(a) *Grant Commitments*

The MSBA has estimated the amount of outstanding Waiting List commitments and New Program commitments at June 30, 2016 to be \$4.8 million and \$1.0 billion, respectively.

(b) *Related Parties*

The MSBA enters into various related party transactions with the Commonwealth. All significant or material transactions have been properly disclosed in the accompanying financial statements.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(c) Operating Lease

The MSBA leases its office space. The lease terminates on June 30, 2025 with future minimum lease payments totaling \$10.3 million as follows:

<u>Fiscal year</u>	<u>Amount</u>
2017	\$ 1,043,111
2018	1,067,703
2019	1,092,295
2020	1,116,887
2021	1,141,479
2022–2026	<u>4,811,835</u>
Total	<u>\$ 10,273,310</u>

Rent expense recorded during fiscal year 2016 was approximately \$899,599.

(9) Intergovernmental Loans

The MSBA has entered into various loan agreements with municipalities at a 2% interest rate, with principal to be paid in equal installments for varying terms. Currently, the longest repayment schedule has a final payment in fiscal year 2043. This program is designed to assist a limited number of school districts with unanticipated inflationary construction costs over the districts' original project budget. The loans outstanding as of June 30, 2016 were \$99.3 million, of which \$6.4 million is due in FY17. During FY16, the MSBA collected \$6.4 million of scheduled principal payments.

On September 23, 2015, the MSBA wrote down the Gateway Regional School District loan receivable by \$2.2 million due to the re-opening of the Russell and Conwell Elementary Schools. The receivable balance as of June 30, 2016 is \$680,799.

(10) Other Post-Employment Benefits

GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions*, requires governments to account for other post-employment benefits, primarily healthcare, on an accrual basis in the government-wide financial statements rather than on a pay-as-you-go basis. The effect is the recognition of an actuarially required contribution as an expense on the statements of activities. To the extent that an entity does not fund their actuarially required contribution, net other post-employment benefit liability is recognized on the statement of net position over time.

(a) Plan Description

The MSBA provides post-employment health care, life insurance, and other post-employment benefits (OPEB) for employees who meet the eligibility criteria and retire directly from the MSBA through the Group Insurance Commission (GIC). The GIC is a state agency that administers an agent multi-employer defined benefit OPEB plan. As of December 31, 2015, the actuarial valuation date, the MSBA had 1 retiree and 58 active plan members. There are 10 terminated employees that have a vested interest to benefits. The plan does not issue a separate financial report.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(b) Benefits Provided

As part of the MSBA employee benefits package administered by the GIC, the MSBA provides health and life insurance to employees who retire from the MSBA and their covered dependents. All active employees who retire from the MSBA, meet the eligibility criteria, and opt for the plan will receive these benefits.

(c) Funding Policy

Subject to statutory requirement, future retirees will contribute 20% of the cost of the premium of the health plan, as determined by the GIC, and the MSBA will contribute the remainder of the health plan costs. The MSBA plans to keep the plan fully funded on an annual basis.

(d) Annual OPEB Costs and Net OPEB Obligation/(Asset)

The MSBA's fiscal year 2016 OPEB expense is calculated based on the value of benefits earned during the year (Normal Cost) and a one-year amortization of the Unfunded Actuarial Accrued Liability (UAAL), as actuarially determined in accordance with the parameters of GASB Statement No. 45. The Annual Required Contribution (ARC) in the table below reflects the full recognition of the UAAL as of June 30, 2016 and 2015. The following table shows the components of the MSBA's OPEB cost for the years ending June 30, 2016 and 2015, the amount actually contributed to the plan, and the change in the MSBA's net OPEB obligation/(asset) based on an actuarial valuation as of December 31, 2015 and December 31, 2012 (amounts in thousands):

	2016	2015
Annual required contribution (ARC)	\$ (282)	(176)
Adjustment to ARC	276	192
Annual OPEB cost	(6)	16
Contributions made	(100)	(100)
Change in net OPEB obligation/(asset)	(106)	(84)
Net OPEB (asset) – beginning of year	(276)	(192)
Net OPEB (asset) – end of year	\$ (382)	(276)

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June 30, 2016

The MSBA's OPEB cost, the percentage of OPEB cost contributed to the plan, and the net OPEB obligation were as follows (amounts in thousands):

<u>Fiscal year ended</u>	<u>OPEB cost</u>	<u>Percentage of OPEB cost contributed</u>	<u>Net OPEB obligation/ (asset)</u>
2016	\$ (6)	Note 1	\$ (382)
2015	16	Note 1	(276)
2014	(9)	Note 1	(192)
2013	(183)	Note 1	(183)
2012	(1,633)	Note 1	—

Note 1: During fiscal year 2012, the MSBA established an irrevocable trust to accumulate assets to pay for future other post-employment benefits. In June 2012, the MSBA contributed \$1,778,000 to the Trust to fully fund it. There was an additional contribution of \$100,000 in fiscal year 2016, and the Trust remains fully funded.

(e) Funded Status and Funding Progress

The funded status of the plan as of January 1, 2016, based on an actuarial valuation as of December 31, 2015, was as follows (amounts in thousands):

Actuarial accrued liability (AAL)	\$ 2,143
Actuarial value of plan assets	<u>2,475</u>
Overfunded actuarial accrued liability (OAAL)	<u><u>\$ (332)</u></u>
Funded ratio (actuarial value of plan assets/AAL)	115.5%
Covered payroll (active plan members)	\$ 5,964
(OAAL) as a percentage of covered payroll	(5.6)%

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

(f) Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the plan as understood by the MSBA and the plan members and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the MSBA and plan members to that

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the December 31, 2015 actuarial valuation, the projected unit credit cost method was used. The actuarial value of assets was determined to be \$2.5 million based on the fair market value of the assets. The actuarial assumptions included an 8.0% investment rate of return and an initial annual healthcare cost trend rate of 6.0%, which decreases to a 5% long-term trend rate for all healthcare benefits after three years. The MSBA has chosen to amortize its AAL over 1 year.

(11) Retirement Benefits

(a) *Plan Description*

The Massachusetts State Employees' Retirement System (MSERS) is a public employee retirement system (PERS) that administers a cost-sharing, multi-employer defined benefit plan as defined by Governmental Accounting Standards Board (GASB) Statement No. 67, *Financial Reporting for Pension Plans*, covering substantially all employees of the Commonwealth and certain employees of the independent authorities and agencies, including employees of MSBA.

Management of MSERS is vested in the Massachusetts State Retirement Board (the MSRB) which consists of five members—two elected by current and active MSERS members, one by the remaining members of the MSRB, one who is appointed by the State Treasurer, and the State Treasurer, who serves as ex-officio and is the Chair of the MSRB.

MSERS Schedule of Employer and Nonemployer Allocations and Schedule of Pension Amounts by Employer and Nonemployer is a publicly available report that can be obtained by submitting a request to the Commonwealth via email to comptroller.info@state.ma.us or mail to: Commonwealth of Massachusetts, Office of the State Comptroller, 1 Ashburton Place, 9th Floor, Boston, Massachusetts, 02108.

(b) *Benefits Provided*

MSERS provides retirement, disability, survivor, and death benefits to members and their beneficiaries. Massachusetts General Laws (MGL) establishes uniform benefit and contribution requirements for all contributory PERS. These requirements provide for superannuation retirement allowance benefits up to a maximum of 80% of a member's highest three-year average annual rate of regular compensation. For employees hired after April 1, 2012, retirement allowances are calculated on the basis of the last five years or any five consecutive years, whichever is greater in terms of compensation. Benefit payments are based upon a member's age, length of creditable service, and group creditable service, and group classification. The authority for amending these provisions rests with the Legislature.

Members become vested after ten years of creditable service. A superannuation retirement allowance may be received upon the completion of twenty years of creditable service or upon reaching the age of 55 with ten years of service. Normal retirement for most employees occurs at age 65; for certain hazardous duty and public safety positions, normal retirement is at age 55. Most employees who joined the system after April 1, 2012 cannot retire prior to age 60.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

The MSERS' funding policies have been established by Chapter 32 of the MGL. The Legislature has the authority to amend these policies. The annuity portion of the MSERS retirement allowance is funded by employees, who contribute a percentage of their regular compensation. Costs of administering the plan are funded out of plan assets.

(c) **Contributions**

Member contributions for MSERS vary depending on the most recent date of membership:

<u>Hire Date</u>	<u>% of Compensation</u>
Prior to 1975	5% of regular compensation
1975–1983	7% of regular compensation
1984 to 6/30/1996	8% of regular compensation
7/1/1996 to present	9% of regular compensation except for State Police which is 12% of regular compensation
1979 to present	An additional 2% of regular compensation in excess of \$30,000

(d) **Pension Liability and Pension Expense**

The net pension liability was measured as of June 30, 2015 (Measurement Date). At June 30, 2016, MSBA was considered to have a 100% special funding situation as defined in the GASB Standards. As such, no net pension liability was required to be recognized by the MSBA. Instead, the Commonwealth is legally obligated for the net pension liability that was associated with MSBA which amounted to \$10.8 million at the Measurement Date.

For the year ended June 30, 2016, MSBA recognized pension expense and intergovernmental revenue of \$1.2 million which represents the Commonwealth's contribution to MSERS on behalf of MSBA.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

Actuarial assumptions. The total pension liability for the June 30, 2015 measurement date was determined by an actuarial valuation as of January 1, 2015, rolled forward to June 30, 2015. This valuation used the following assumptions:

Inflation	3.5%
Salary increases	Salary increases are based on analyses of past experience, but range from 3.5% to 9.0%, depending on group and length of service.
Investment rate of return	7.50%
Cost of living adjustments	3.0% cost of living increase per year
Mortality rates:	
Pre-retirement:	Reflects RP-2000 Employees table projected generationally with Scale BB and a base year of 2009 (gender distinct).
Healthy retiree:	Reflects Healthy Annuitant table projected generationally with Scale BB and a base year of 2009 (gender distinct).
Disabled retiree:	The mortality rate is assumed to be in accordance with the RP-2000 Table projected generationally, with Scale BB and a base year of 2015 (gender distinct).

Investment assets of MSERS are with the Pension Reserves Investment Trust (PRIT) Fund. The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future rates of return by the target asset allocation percentage. Best estimates of geometric rates of return for each major asset class included in the PRIT Fund's target asset allocation as of June 30, 2015 are summarized in the following table:

Asset class	Target allocation (%)	Long-term expected rate of return (%)
Global equity	40%	6.9%
Core fixed income	13	2.4
Private equity	10	8.5
Real estate	10	6.5
Value added fixed income	10	5.8
Hedge Funds	9	5.8
Portfolio Completion Strategies	4	5.5
Timber/natural resources	4	6.6
	<u>100</u>	

MASSACHUSETTS SCHOOL BUILDING AUTHORITY

Notes to Financial Statements

June 30, 2016

(e) Discount Rate

The discount rate used to measure the total pension liability was 7.5%. The projection of cash flows used to determine the discount rate assumed that Plan member contributions will be made at the current contribution rates and the Commonwealth's contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rates. Based on those assumptions, the net position was projected to be available to make all projected future benefit payments of current Plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

(f) Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the MSBA's proportion of the net pension liability, calculated using the discount rate of 7.5%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (6.5%) or 1-percentage-point higher (8.5%) than the current discount rate (amount in thousands):

	<u>1% Decrease (6.5%)</u>	<u>Current discount (7.5%)</u>	<u>1% Increase (8.5%)</u>
Net pension liability as of June 30, 2015	\$ 14,718	10,827	7,472

(12) Subsequent Events

On August 25, 2016, the MSBA used funds on hand to defease \$15.0 million of the 2009 Series A Dedicated Sales Tax Bonds outstanding.

On October 26, 2016, the MSBA issued \$405.0 million of Senior Dedicated Sales Tax Bonds (2016 Series B Bonds). The Bonds mature at various dates through November 2046 and interest is due semi-annually each May 15th and November 15th. The interest rate on the bonds ranges from 2% to 5%.

On October 26, 2016, the MSBA refunded \$216.0 million of 2007 Dedicated Sales Tax Bonds by issuing \$188.6 million of Senior Sales Tax Refunding Bonds (2016 Series C Bonds). The Bonds mature on November 15, 2035 and the interest on the bonds is payable semi-annually on May 15th and November 15th. The coupons on the bonds range from 4% to 5%. The refunding resulted in reduced debt service of \$44.8 million and a present value savings of \$31.3 million over the life of the debt.

MASSACHUSETTS SCHOOL BUILDING AUTHORITY
Schedule of Funding Progress – Required Supplementary Information
June 30, 2016
(Unaudited)
(Dollars in thousands)

Other postemployment benefits						
Actuarial valuation	Assets (a)	Actuarial accrued liability (AAL) (b)	Unfunded AAL (UAAL) (b-a)	Funded ratio (a/b)	Covered payroll (c)	UAAL as a percentage of covered payroll ((b-a)/(c))
January 1, 2016	\$ 2,475	2,143	(331)	115.5%	\$ 5,964	—
January 1, 2015	2,460	2,232	(228)	110.2	5,206	—
January 1, 2014	2,189	1,941	(248)	112.8	4,880	—
January 1, 2013	1,909	1,668	(241)	114.4	4,490	—

MASSACHUSETTS SCHOOL BUILDING AUTHORITY
Schedule of Employer Contributions – Required Supplementary Information
June 30, 2016
(Unaudited)
(Dollars in thousands)

Other postemployment benefits			
Fiscal year ending June 30	Annual OPEB costs	Actual contributions	Percentage contributed
2016	\$ (6)	\$ 100	(158)
2015	16	100	625
2014	(9)	—	—
2013	(183)	—	—

See accompanying independent auditors' report.



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Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

The Board Members
Massachusetts School Building Authority:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Massachusetts School Building Authority (the Authority), a blended component of the Commonwealth of Massachusetts, as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated December 14, 2016.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The



results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

KPMG LLP

Boston, Massachusetts
December 14, 2016