PENNICHUCK

March 28, 2014

ANNUAL REPORT TO THE SHAREHOLDER

Dear Shareholder:

The Annual Meeting of Pennichuck Corporation will be held at 8:30 a.m. on Saturday, May 10, 2014 at the Courtyard Marriott, 2200 Southwood Drive, Nashua, New Hampshire.

Background on the City's Acquisition and Our Corporate Structure. The City's acquisition of the shares of Pennichuck Corporation was completed on January 25, 2012 ending a long standing dispute between Pennichuck Corporation and the City of Nashua. As part of the acquisition, the corporate structure of Pennichuck Corporation and its utility subsidiaries was retained. Under this structure, the City of Nashua is the sole shareholder of Pennichuck Corporation. Under the Company's By-Laws, the City in its capacity as shareholder makes its decisions through actions by its Board of Aldermen, in accordance with the City's Charter. No single person – the Mayor or any individual member of the Board of Aldermen – is him or herself a shareholder; rather, the entity of the City itself is the sole shareholder of Pennichuck Corporation represented by the Board of Aldermen and the Mayor.

Pennichuck continues to own its five corporate subsidiaries, including its three regulated public utilities (Pennichuck Water Works, Inc., Pennichuck East Utility, Inc., and Pittsfield Aqueduct Company, Inc.), a service company (Pennichuck Water Service Corporation), and its real estate company (The Southwood Corporation).

As unanimously approved by the City's Board of Aldermen at the time of the acquisition, this corporate structure was retained for several reasons.

First, the City's Mayor and Board of Aldermen desired to maintain some stability and continuity for all of the customers and employees of the Pennichuck companies. Retaining the existing corporate structure minimized the need for any radical changes to the utility companies and operations and encouraged support by all of the communities served by the utilities.

Second, retaining the corporate structure provided continuity for the regulatory and financial status of the corporations and their respective businesses. The New Hampshire Public Utilities Commission will continue to provide regulatory oversight for the utility companies, and banks, lenders and other contract parties will continue to be able to rely on existing contracts and other rules with respect to financing and other operations.

Third, the Mayor and Board of Aldermen unanimously agreed to establish a corporate governance system for the purposes of managing Pennichuck Corporation. This corporate governance system relies upon well-established principles of corporate law, and is established pursuant to Pennichuck Corporation's Articles of Incorporation and By-Laws, as adopted by the City and the Company at the time of the acquisition pursuant to the Merger Agreement.

This well-known corporate governance model, which incorporates well-established principles regarding fiduciary obligations of board members, was structured to provide assurances to the City's rating agencies, potential lenders, the New Hampshire Public Utilities Commission and the many communities we serve that decisions will be made based on sound business and financial analysis, and in a manner that minimizes political considerations.

Our Operations, Our Communities and Our Customers. Our companies provide water service to a wide range of communities and customers.

Pennichuck Water Works, Inc. provides water service to approximately 27,000 customers in 11 communities which include Amherst, Bedford, Derry, Epping, Hollis, Merrimack, Milford, Nashua, Newmarket, Plaistow and Salem.

Pennichuck East Utility, Inc. provides water service to approximately 7,000 customers in 19 communities which include Atkinson, Barnstead, Bow, Chester, Conway, Derry, Exeter, Hooksett, Lee, Litchfield, Londonderry, Middleton, Pelham, Plaistow, Raymond, Sandown, Tilton, Weare and Windham.

Pittsfield Aqueduct Company, Inc. provides water service to approximately 600 customers in Pittsfield.

Pennichuck Water Service Corporation provides service in connection with the management of water services for two communities; billing, collection and customer services for three communities; and water meter testing services, as well as contracted water services at various levels for approximately 85 small independently owned water systems.

The Southwood Corporation owns various parcels of land in the Town of Merrimack.

The Company's mission is to be a premier supplier of water in New Hampshire by providing reliable, high quality and affordable water in sufficient quantities and be New England's premier supplier of water related contract services by providing high quality solutions to meet our customers' needs. Strategies supporting the mission have been developed relative to our water resources, employees, financing, customer services and Company assets. These strategies together with the goals and plans to support the strategies are available on the Company's website, www.pennichuck.com, under the "Company Reports" caption.

The Company currently has 106 employees. Each of the employees is committed to supporting the Company's mission. Each of our managers has goals and objectives to support the strategies supporting the mission.

Financial Performance During the Last Year. The Company's audited consolidated financial statements for the year ended December 31, 2013 are attached to this report.

	($ Millions)			
	4th Quarter		Year to Date	
	2012	2013	2012	2013
Revenues	$ 8.2	$ 8.5	$37.8	$37.7
Operating Expenses	(6.9)	(7.3)	(28.6)	(30.3)
Operating Income	1.3	1.2	9.2	7.4
Interest Expense	(2.6)	(2.5)	(9.6)	(10.1)
Non-Operating Expenses	-	-	(3.8)	-
Other Income	-	-	1.6	0.9
Pre-Tax Income (Loss)	(1.3)	(1.3)	(2.6)	(1.8)
Income Taxes Expense (Benefit)	(.1)	(0.9)	(0.7)	(0.8)
Net Income (Loss)	(1.2)	(0.4)	(1.9)	(1.0)
Dividends Paid to the Shareholder	-	0.5	0.2	0.8
Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA)	2.6	2.9	12.3	15.3

- Consolidated revenues for the quarter increased by $0.3 million from $8.2 million in 2012 to $8.5 million in 2013. The increase is partially attributable to the temporary rate increases approved by the New Hampshire Public Utilities Commission in November 2013 for Pennichuck East Utility, Inc. and Pittsfield Aqueduct Company, Inc.

- Consolidated year to date revenues decreased slightly from $37.8 million in 2012 to $37.7 million in 2013. Revenues from the regulated utilities decreased from $35.1 million in 2012 to $34.8 million in 2013. The decrease was mainly attributable to the wet weather conditions in the May/June time frame. Revenues from the unregulated water service company partially offset the decline in revenues from the regulated utilities. Revenues from the water service company increased from $2.7 million in 2012 to $2.9 million in 2013.

- Consolidated operating expenses increased by $0.4 million during the fourth quarter. The increase was partially due to the increased amortization of the acquisition premium described below.

- Consolidated operating expenses increased by $1.7 million or 5.9% from 2012 to 2013. The major components of the increases for the year to date expenses are as follows:

    - The amortization of the acquisition premium paid for the Company in the merger transaction, known as the Municipal Acquisition Regulatory Asset, increased by $1.5 million in 2013. The amortization is a non-cash item. (Refer to Note 10 in the attached December 31, 2013 Audited Consolidated Financial Statements for further information.)

    - Approximately $214,000 increase in state utility and local property taxes for 2013 versus 2012. The utility and local property tax expense increased from $4.3 million in 2012 to $4.5 million in 2013.

- Approximately $3.8 million of merger related costs were recorded in 2012. These costs in 2012 were related to severance for former senior management personnel, as well as transaction related investment banker fees and directors and officers insurance premiums. Although these costs were recorded per generally accepted accounting principles (GAAP), they were funded as a part of the merger transaction.

- Approximately $1.6 million of other income was realized in 2012 relating to the sale of land, and includes the recognition of the gain from the sale, after recognizing the write-off of the cost basis of the underlying assets, and the payment of property taxes from the conversion from current use. Approximately $0.9 million was realized in 2013 from the sale of a conservation easement to the Society for the Protection of New Hampshire Forests on land located in Merrimack, NH.

- An increase in interest expense from 2012 to 2013 of approximately $0.5 million is primarily attributed to the interest on the note payable to the City, resulting from the merger transaction. The Company paid interest for twelve months in 2013 versus eleven months in 2012.

Capital Expenditures

Capital expenditures in the fourth quarter of 2013 were $2.6 million compared to $2.1 million in the fourth quarter of 2012. For the year 2013, capital expenditures were $6.6 million as compared to $6.4 million in 2012.

The major expenditures for 2013 were as follows:

	($000's)
Meters (all utilities)	$ 743
Liberty Tree – Replacement Structure (PEU – Raymond)	581
Replacement of Carbon Media – Water Treatment Plant	435
Franklin Street Main Replacement (Nashua)	406
Middle Street Main Replacement (Amherst)	325
Locke Lake Pipe Replacement (PEU – Barnstead)	320
Asset Management and GIS System Implementation	301
Data Presentation (DPaC Work Order Project)	298
Hillcrest Street Main Replacement (Nashua)	253
Baldwin Street Main Replacement (Nashua)	244
Vehicles	228
Walnut Street Main Replacement (Nashua)	183
Fairmount Street Main Replacement (Nashua)	178
Ash Street Main Replacement (Nashua)	166
Berry Brook Dam Removal (PAC – Pittsfield)	129
Pleasant Street Main Replacement (Nashua)	119

Regulated Utilities Rate Cases

As required in the Public Utilities Commission's (PUC) approval of the Pennichuck acquisition by the City of Nashua, the Pennichuck regulated utilities each filed rate cases simultaneously on May 31, 2013. Filings with the PUC are available on the Company's website (www.Pennichuck.com) under the "Company Reports" caption. The PUC approved a 7% temporary rate increase for Pittsfield Aqueduct Company, Inc. on November 22, 2013 (Order No. 25,599) and a 7% temporary rate increase for Pennichuck East Utility, Inc. on November 27, 2013 (Order No. 25,602). PUC hearings on permanent rates for each of the regulated utilities are scheduled for May 20, 2014.

Conservation Easement

The Company placed 218 acres of land in Merrimack in a permanent conservation easement with the Society for the Protection of New Hampshire Forests on July 18, 2013. Income in the amount of $891,000 was recognized by the sale of this easement.

Succession Planning

In July 2013, the Board of Directors extended the employment of John Patenaude as the Company's Chief Executive Officer through November 2015. Mr. Patenaude accepted the Board's offer. As part of the Board's succession planning efforts, the Compensation and Benefits Committee of the Board of Directors and the full Board have adopted a process for selecting a Chief Executive Officer. The CEO Succession Plan Process can be viewed on Pennichuck's website (www.Pennichuck.com) under the "Board of Directors" caption.

Company Goals – 2014

The Company's main goals for 2014 are as follows:

- continue to provide excellent water quality and services;
- continue prudent investments in the aging infrastructure;
- continue investments and training in IT Systems to increase the efficiency of operations; and
- market the services of the water service company relative to meter testing and customer billings and services.

Other detailed information is included in the Company's financial statements.

Sincerely,

John L. Patenaude
Chief Executive Officer

Pennichuck Corporation and Subsidiaries

Audited Consolidated Financial Statements

December 31, 2013 and 2012

Contents

MH&Co

MELANSON HEATH & COMPANY, PC
CERTIFIED PUBLIC ACCOUNTANTS
MANAGEMENT ADVISORS

INDEPENDENT AUDITORS' REPORT

Board of Directors and Stockholder
Pennichuck Corporation and Subsidiaries

We have audited the accompanying consolidated financial statements of Pennichuck Corporation and Subsidiaries, which comprise the consolidated balance sheets as of December 31, 2013 and 2012, and the related consolidated statements of income, comprehensive income, changes in stockholder's equity, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

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Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Pennichuck Corporation and Subsidiaries as of December 31, 2013 and 2012, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Melanson, Heath + Company P.C.

Nashua, New Hampshire
March 19, 2014

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
As of December 31, 2013 and 2012
(in thousands, except share data)

	2013	2012
ASSETS		
Property, Plant and Equipment, net	$ 167,711	$ 164,058
Current Assets:		
Cash and cash equivalents	1,038	873
Restricted cash	5,563	5,443
Accounts receivable - billed, net	2,301	2,380
Accounts receivable - unbilled, net	2,102	1,991
Accounts receivable - other	34	-
Inventory	820	751
Prepaid expenses	528	485
Prepaid property taxes	1,034	881
Deferred and refundable income taxes	-	148
Total Current Assets	13,420	12,952
Other Assets:		
Deferred land costs	2,251	2,251
Debt issuance expenses	3,406	3,623
Investment in real estate partnership	110	113
Other	5,583	10,272
Acquisition premium	80,719	83,261
Total Other Assets	92,069	99,520
TOTAL ASSETS	$ 273,200	$ 276,530

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS - CONTINUED
As of December 31, 2013 and 2012
(in thousands, except share data)

	2013	2012
STOCKHOLDER'S EQUITY AND LIABILITIES		
Stockholder's Equity:		
Common stock; $0.01 par value; 1,000 shares authorized, issued and outstanding	$ -	$ -
Additional paid in capital	30,561	30,561
Accumulated deficit	(4,099)	(2,366)
Accumulated other comprehensive income	298	35
Total Shareholder's Equity	26,760	28,230
Long-Term Debt, Less Current Portion	174,431	174,279
Current Liabilities:		
Line of credit	1,966	-
Current portion of long-term debt	2,965	2,780
Accounts payable	1,150	908
Accrued property taxes	13	57
Deferred revenue	66	61
Accrued interest payable	576	618
Other accrued expenses	212	127
Accrued wages and payroll withholding	282	262
Customer deposits and other	111	137
Total Current Liabilities	7,341	4,950
Other Liabilities and Deferred Credits:		
Deferred income taxes	19,807	20,625
Accrued pension liability	5,257	8,855
Unamortized debt premium	427	464
Deferred investment tax credits	636	669
Regulatory liability	824	846
Accrued post-retirement benefits	1,858	2,368
Customer advances	84	84
Contributions in aid of construction, net	34,686	33,533
Derivative instrument	386	825
Other long-term liabilities	703	802
Total Other Liabilities and Deferred Credits	64,668	69,071
TOTAL STOCKHOLDER'S EQUITY AND LIABILITIES	$ 273,200	276,530

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
For the Years Ended December 31, 2013 and 2012
(in thousands)

	2013	2012
Operating Revenues	$ 37,694	$ 37,756
Operating Expenses:		
Operations and maintenance	18,523	18,540
Depreciation and amortization	6,661	5,173
Taxes other than income taxes	5,072	4,857
Total Operating Expenses	30,256	28,570
Operating Income	7,438	9,186
Merger-related Costs	-	(3,750)
Interest Expense	(10,128)	(9,615)
Gain on Sale of Land	-	1,629
Allowance for Funds Used During Construction	14	-
Other, Net	872	(32)
Loss Before Benefit From Income Taxes	(1,804)	(2,582)
Benefit From Income Taxes	848	680
Net Loss	$ (956)	$ (1,902)

The accompanying notes are an integral part of these consolidated financial statements

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
For the Years Ended December 31, 2013 and 2012
(in thousands)

	2013	2012
Net Loss	$ (956)	$ (1,902)
Other Comprehensive Income (Loss):		
Unrealized gain (loss) on derivatives	283	(149)
Reclassification of net loss realized in net income	156	157
Retirement of old capital structure due to change in control	-	530
Income tax benefit relating to other comprehensive income	(176)	(3)
Other Comprehensive Income (Loss)	263	535
Comprehensive Loss	$ (693)	$ (1,367)

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDER'S EQUITY
(in thousands, except per share data)

	Common Stock		Additional Paid in Capital	Retained Earnings/(Deficit)	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount				
Balance as of January 1, 2013	1,000	$ -	$ 30,561	$ (2,366)	$ 35	$ 28,230
Common dividends declared-$208.266 per share	-	-	-	(777)	-	(777)
Net loss	-	-	-	(956)	-	(956)
Other comprehensive income (loss):						
Unrealized gain on derivatives, net of taxes of $113	-	-	-	-	170	170
Reclassification of net loss realized in net income, net of taxes of $63	-	-	-	-	93	93
Balance as of December 31, 2013	1,000	$ -	$ 30,561	$ (4,099)	$ 298	$ 26,760

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDER'S EQUITY
(in thousands, except per share data)

	Common Stock		Additional Paid in Capital	Retained Earnings/(Deficit)	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
	Shares	Amount					
Balance as of January 1, 2012	4,695,757	$ 4,696	$ 41,689	$ 11,132	$ (500)	$ (138)	$ 56,879
Exercise of stock options	1,067	1	20	-	-	-	21
Stock-based compensation	-	-	56	-	-	-	56
Retirement of old capital structure due to change in control	(4,696,824)	(4,697)	(41,765)	(11,386)	530	138	(57,180)
Issuance of common shares under new capital structure	1,000	-	30,561	-	-	-	30,561
Common dividends declared-$209.934 per share	-	-	-	(210)	-	-	(210)
Net loss	-	-	-	(1,902)	-	-	(1,902)
Other comprehensive income (loss):							
Unrealized loss on derivatives, net of taxes of $(60)	-	-	-	-	(89)	-	(89)
Reclassification of net loss realized in net income, net of taxes of $63	-	-	-	-	94	-	94
Balance as of December 31, 2012	1,000	$ -	$ 30,561	$ (2,366)	$ 35	$ -	$ 28,230

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2013 and 2012
(in thousands)

	2013	2012
Operating Activities:		
Net Loss	$ (956)	$ (1,902)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	6,949	5,438
Amortization of original issue discount	12	12
Equity component of AFUDC	(8)	-
Amortization of deferred investment tax credits	(33)	(33)
Provision for deferred income tax	(994)	(13)
Undistributed loss in real estate partnership	5	6
Stock-based compensation expense	-	56
Changes in assets and liabilities:		
(Increase) decrease in accounts receivable and unbilled revenue	(83)	1,207
(Increase) decrease in materials and supplies	(69)	63
(Increase) decrease in prepaid expenses	(196)	467
Decrease in deferred charges and other assets	5,180	491
(Increase) decrease in refundable income taxes	155	(79)
Increase (decrease) in accounts payable and deferred revenue	257	(161)
Decrease in accrued interest payable	(42)	(130)
Increase (decrease) in other	(4,194)	1,654
Net cash provided by operating activities	5,983	7,076
Investing Activities:		
Purchase of property, plant and equipment including debt component of allowance for funds used during construction	(7,270)	(6,980)
Increase in restricted cash	(120)	(5,443)
Payments made in connection with merger-related activities	-	(143,971)
Change in investment in real estate partnership and deferred land costs	(3)	294
Net cash used in investing activities	$ (7,393)	$ (156,100)

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2013 and 2012
(in thousands)

	2013	2012
Financing Activities:		
Borrowings on line of credit	$ 1,966	$ -
Payments on long term debt	(2,835)	(3,697)
Contributions in aid of construction	93	55
Proceeds from long term borrowings	3,161	120,209
Debt issuance costs	(33)	(30)
Proceeds from issuance of common stock and dividend reinvestment plan	-	30,583
Dividends paid	(777)	(210)
Net cash provided by financing activities	1,575	146,910
Increase (decrease) in cash and cash equivalents	165	(2,114)
Cash and cash equivalents, beginning of period	873	2,987
Cash and cash equivalents, end of period	$ 1,038	$ 873

Supplemental Disclosure on Cash Flow and Non-cash Items
For the Years Ended December 31, 2013 and 2012 (in thousands)

	2013	2012
Cash paid (refunded) during the period for:		
Interest	$ 9,937	$ 9,512
Income taxes	81	186
Non-cash items:		
Contributions in aid of construction	1,825	1,133
Forgiveness of debt	56	42

The accompanying notes are an integral part of these consolidated financial statements.

PENNICHUCK CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 – Description of Business and Summary of Significant Accounting Policies

Description of Business:

Pennichuck Corporation (our "Company," "we," or "our") is a holding company headquartered in Merrimack, New Hampshire with five wholly owned operating subsidiaries: Pennichuck Water Works, Inc., ("Pennichuck Water") Pennichuck East Utility, Inc., ("Pennichuck East") and Pittsfield Aqueduct Company, Inc. ("PAC") (collectively referred to as our Company's "utility subsidiaries"), which are involved in regulated water supply and distribution to customers in New Hampshire; Pennichuck Water Service Corporation ("Service Corporation") which conducts non-regulated water-related services; and The Southwood Corporation ("Southwood") which owns several parcels of undeveloped land.

Our Company's utility subsidiaries are engaged principally in the collection, storage, treatment and distribution of potable water to approximately 34,900 customers throughout the State of New Hampshire. The utility subsidiaries, which are regulated by the New Hampshire Public Utilities Commission (the "NHPUC"), are subject to the provisions of Accounting Standards Codification ("ASC") Topic 980 "*Regulated Operations.*"

Summary of Significant Accounting Policies:

Basis of Presentation

The accompanying consolidated financial statements include the accounts of our Company and its wholly owned subsidiaries. All significant intercompany transactions have been eliminated in consolidation.

Use of Estimates in the Preparation of Financial Statements

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

Property, Plant and Equipment

Property, plant and equipment, which includes principally the water utility assets of our Company's utility subsidiaries, is recorded at cost plus an allowance for funds used during construction on major, long-term projects and includes property funded with contributions in aid of construction.

Maintenance, repairs and minor improvements are charged to expense as incurred. Improvements which significantly increase the value of property, plant and equipment are capitalized.

Cash and Cash Equivalents

Cash and cash equivalents generally consist of cash, money market funds and other short-term liquid investments with original maturities of three months or less.

Restricted Cash

Restricted cash consists of funds maintained for the Rate Stabilization Fund ("RSF"), which was established in conformity with the requirements of New Hampshire Public Utilities Commission ("NHPUC") Order 25,292, as explained more fully in Note 10 of these financial statements. The RSF is an imprest fund of $5,000,000, which is subject to funding above or below the imprest fund balance, reflecting actual revenue performance as it relates to prescribed revenue levels supported by the RSF. Of the approximately $5.6 million in restricted cash as of December 31, 2013, and in compliance with the rules governing the use of the RSF, approximately $448,000 is slated to be returned to rate payers as a component of the new water rates set as a result of the settlement of the current rate cases before the NHPUC for the 2012 test year. Upon receipt of a final rate order in late 2014 for these current rate cases, this amount will become unrestricted cash.

Concentration of Credit Risks

Financial instruments that subject our Company to credit risk consist primarily of cash and accounts receivable. Our cash balances are invested in a financial institution insured to statutory limit by the Federal Deposit Insurance Corporation ("FDIC"). Our accounts receivable balances primarily represent amounts due from the residential, commercial and industrial customers of our regulated water utility operations as well as receivables from our Service Corporation customers.

Accounts Receivable - Billed

Accounts receivable are recorded at the invoiced amounts. The allowance for doubtful accounts is our best estimate of the amount of probable credit losses in our existing accounts receivable, and is determined based on historical write-off experience and the aging of account balances. We review the allowance for doubtful accounts quarterly. Account balances are written off against the allowance when it is probable the receivable will not be recovered.

Accounts Receivable - Unbilled

We read our customer meters on a monthly basis and record revenues based on meter reading results. Information from the last meter reading date is used to estimate the value of unbilled revenues through the end of the accounting period. Estimates of water utility revenues for water delivered to customers but not yet billed are accrued at the end of each accounting period. Actual results could differ from those estimates.

Inventory

Inventory is stated at the lower of cost, using the average cost method, or market.

Deferred Land Costs

Included in deferred land costs is our Company's original basis in its undeveloped land-holdings and any land improvement costs, which are stated at the lower of cost or market. All costs associated with real estate and land projects are capitalized and allocated to the project to which the costs relate. Administrative labor and the related fringe benefit costs attributable to the acquisition, active development and construction of land parcels are capitalized as deferred land costs. No labor and benefits were capitalized for the years ended December 31, 2013 and 2012.

Deferred Charges and Other Assets

Deferred charges include certain regulatory assets and costs of obtaining debt financing. Regulatory assets are amortized over the periods they are recovered through NHPUC-authorized water rates. Deferred financing costs are amortized over the term of the related bonds and notes. Our Company's utility subsidiaries have recorded certain regulatory assets in cases where the NHPUC has permitted, or is expected to permit, recovery of these costs over future periods. Currently, the regulatory assets are being amortized over periods ranging from 3 to 25 years.

Contributions in Aid of Construction ("CIAC")

Under construction contracts with real estate developers and others, our Company's utility subsidiaries may receive non-refundable advances for the cost of installing new water mains. These advances are recorded as CIAC. The utility subsidiaries also record to plant and CIAC the fair market value of developer installed mains and any excess of fair market value over the cost of community water systems purchased from developers. CIAC are amortized over the life of the property.

Revenues

Standard charges for water utility services to customers are recorded as revenue, based upon meter readings and contract service, as services are provided. The majority of our Company's water revenues are based on rates approved by the NHPUC. Estimates of unbilled service revenues are recorded in the period the services are provided. Provision is made in the financial statements for estimated uncollectible accounts.

Non-regulated water management services include contract operations and maintenance, and water testing and billing services to municipalities and small, privately owned community water systems. Contract revenues are billed and recognized on a monthly recurring basis in accordance with agreed-upon contract rates. Revenues from unplanned additional work are based upon time and materials incurred in connection with activities not specifically identified in the contract, or for which work levels exceed contracted amounts.

Revenues from real estate operations, other than undistributed earnings or losses from equity method joint ventures, are recorded upon completion of a sale of real property. Our Company's real estate holdings outside of our regulated utilities are comprised primarily of undeveloped land.

Investment in Joint Venture

Southwood uses the equity method of accounting for its investment in a joint venture in which it does not have a controlling interest. Under this method, Southwood records its proportionate share of losses under "Other, net" in the accompanying Consolidated Statements of Income with a corresponding decrease in the carrying value of the investment.

Income Taxes

Income taxes are recorded using the accrual method and the provision for federal and state income taxes is based on income reported in the consolidated financial statements, adjusted for items not recognized for income tax purposes. Provisions for deferred income taxes are recognized for accelerated depreciation and other temporary differences. A valuation allowance is provided to offset any net deferred tax assets if, based upon available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. Investment tax credits previously realized for income tax purposes are amortized for financial statement purposes over the life of the property, giving rise to the credit.

Recently Issued Accounting Standards

We do not expect the adoption of any recently issued accounting pronouncements to have a material impact on our financial condition or results of operations.

Note 2 – Property, Plant and Equipment

The components of property, plant and equipment as of December 31, 2013 and 2012 were as follows:

(in thousands)	2013	2012	Useful Lives (in years)
Utility Property:			
Land and land rights	$ 2,927	$ 2,911	-
Source of supply	50,399	50,027	12 - 75
Pumping and purification	29,775	28,794	14 - 64
Transmission and distribution, including services, meters and hydrants	124,024	119,638	15 - 91
General and other equipment	10,142	10,206	7 - 75
Intangible plant	768	766	20
Construction work in progress	2,524	1,063	
Total utility property	220,559	213,405	
Total non-utility property	5	5	5 - 10
Total property, plant and equipment	220,564	213,410	
Less accumulated depreciation	(52,853)	(49,352)	
Property, plant and equipment, net	$ 167,711	$ 164,058	

The provision for depreciation is computed on the straight-line method over the estimated useful lives of the assets which range from 5 to 91 years. The weighted average composite depreciation rate was 2.45% and 2.48% in 2013 and 2012, respectively.

Note 3 – Accounts Receivable

Accounts receivable consisted of the following at December 31, 2013 and 2012:

(in thousands)	2013	2012
Accounts receivable - billed	$ 2,345	$ 2,426
Less allowance for doubtful accounts	(44)	(46)
Accounts Receivable - billed, net	$ 2,301	$ 2,380
Accounts receivable - unbilled	$ 2,102	$ 1,991
Less allowance for doubtful accounts	-	-
Accounts Receivable - unbilled, net	$ 2,102	$ 1,991

Note 4 – Deferred Charges and Other Assets

Deferred charges and other assets as of December 31, 2013 and 2012 consisted of the following:

(in thousands)	2013	2012	Recovery Period (in years)
Regulatory assets:			
Source development charges	$ 764	$ 820	5 - 25
Miscellaneous studies	852	608	3 - 25
Unrecovered pension and post-retirement benefits expense	3,342	8,096	(1)
Total regulatory assets	4,958	9,524	
Supplemental executive retirement plan asset	625	748	
Subtotal	5,583	10,272	
Debt issuance expenses	3,406	3,623	(1)
Total deferred charges and other assets	$ 8,989	$ 13,895	

(1) We expect to recover these amounts consistent with the anticipated expense recognition of these assets.

Note 5 – Post-retirement Benefit Plans

Pension Plan and Other Post-retirement Benefits

We have a non-contributory, defined benefit pension plan (the "DB Plan") that covers substantially all employees. The benefits are based on years of service and participant compensation levels. Our funding policy is to contribute annual amounts that meet the requirements for funding under the U.S. Department of Labor's Pension Protection Act. Contributions are intended to provide not only for benefits attributed to service to date but also for those expected to be earned in the future.

We provide post-retirement medical benefits for eligible retired employees through one of two plans (collectively referred to as our "OPEB Plans"). For employees who retire on or after the normal retirement age of 65, benefits are provided through a post-retirement plan (the "Post-65 Plan"). For eligible non-union employees who retire prior to their normal retirement age and who have met certain age and service requirements, benefits are provided through a post-employment medical plan (the "Post-employment Plan"). Future benefits under the Post-65 Plan increase annually based on the actual percentage of wage and salary increases earned from the plan inception date to the normal retirement date. The benefits under the Post-employment Plan allow for the continuity of medical benefits coverage at group rates from the employee's retirement date until the employee becomes eligible for Medicare. The OPEB Plans are funded from the general assets of our Company.

Upon retirement, if a qualifying employee elects to receive medical benefits under one of our OPEB Plans, we pay up to a maximum monthly benefit of $307 based on years of service.

The following table sets forth information regarding our DB Plan and our OPEB Plans as of December 31, 2013 and for the year then ended:

(in thousands)	DB Plan	OPEB Plans
Projected benefit obligations	$ 17,501	$ 2,809
Employer contribution	911	22
Benefits paid, excluding expenses	(410)	(36)
Fair value of plan assets	12,244	944
Accumulated benefit obligation	15,665	-
Funded status	(5,257)	(1,879)
Net periodic benefit cost	1,372	204
Amount of the funded status recognized in the Consolidated Balance Sheet consisted of:		
Current liability	$ -	$ (21)
Non-current liability	(5,257)	(1,858)
Total	$ (5,257)	$ (1,879)

The following table sets forth information regarding our DB Plan and our OPEB Plans as of December 31, 2012, and for the year then ended:

(in thousands)	DB Plan	OPEB Plans
Projected benefit obligations	$ 18,569	$ 3,212
Employer contribution	983	49
Benefits paid, excluding expenses	(369)	(49)
Fair value of plan assets	9,713	818
Accumulated benefit obligation	16,158	-
Funded status	(8,855)	(2,394)
Net periodic benefit cost	1,388	180
Amount of the funded status recognized in the Consolidated Balance Sheet consisted of:		
Current liability	$ -	$ (26)
Non-current liability	(8,855)	(2,368)
Total	$ (8,855)	$ (2,394)

Changes in plan assets and benefit obligations recognized in regulatory assets, for the year ended December 31, 2013, were as follows:

(in thousands)	DB Plan	OPEB Plans
Regulatory asset balance, beginning of period	$ 7,874	$ 222
Net actuarial loss/(gain) incurred during the period	(3,641)	(699)
Prior service cost incurred during the period	-	-
Recognized net actuarial (gain)/loss	(418)	4
Regulatory asset balance, end of period	$ 3,815	$ (473)

Changes in plan assets and benefit obligations recognized in regulatory assets, for the year ended December 31, 2012, were as follows:

(in thousands)	DB Plan	OPEB Plans
Regulatory asset balance, beginning of period	$ 6,907	$ 1,208
Net actuarial loss/(gain) incurred during the period	1,352	(212)
Prior service cost incurred during the period	-	(785)
Recognized net actuarial (gain)/loss	(385)	11
Regulatory asset balance, end of period	$ 7,874	$ 222

The reduction in prior service cost recognized during 2012, as shown in the table above in the amount of $785,000, resulted from changes to certain underlying factors relating to future benefit costs, relating to one of the OPEB plans. The Post-65 Plan was changed as of January 1, 2012 relating to the cost of underlying health insurance premiums for the plan, as well as a clearer definition of the basis for premium amounts anticipated for employees already collecting benefits from the plan, as well as future benefits to be earned by employees eligible under the plan, for which benefits have not yet been paid out. The resulting decrease in the liability of $785,000 will be amortized over the future working lifetime of active employees.

Amounts recognized in regulatory assets for the DB and OPEB Plans that have not yet been recognized as components of net periodic benefit cost of the following as of December 31, 2013:

(in thousands)	DB Plan	OPEB Plans
Net actuarial (gain)/loss	$ 3,815	$ (311)
Prior service cost	-	(162)
Regulatory asset	$ 3,815	$ (473)

Amounts recognized in regulatory assets for the DB and OPEB Plans that have not yet been recognized as components of net periodic benefit cost of the following as of December 31, 2012:

(in thousands)	DB Plan	OPEB Plans
Net actuarial (gain)/loss	$ 7,874	$ 384
Prior service cost	-	(162)
Regulatory asset	$ 7,874	$ 222

The key assumptions used to value benefit obligations and calculate net periodic benefit cost for our DB and OPEB Plans include the following:

	2013	2012
Discount rate for net periodic benefit cost, beginning of year	4.00%	4.50%
Discount rate for benefit obligations, end of year (a)	4.84%	4.00%
Expected return on plan assets for the period (net of investment expenses)	7.50%	7.50%
Rate of compensation increase, beginning of year	2.75%	3.00%
Healthcare cost trend rate (applicable only to OPEB Plans)	9.50%	10.00%

(a) An increase or decrease in the discount rate of 0.5% would result in a change in the funded status as of December 31, 2013, for the DB Plan and the OPEB Plans of approximately $1.33 million and $257 thousand, respectively.

The estimated net actuarial loss for our DB Plan that will be amortized in 2014 from the regulatory assets into net periodic benefit costs is $175,000. The estimated net actuarial loss and prior service cost for our OPEB Plans that will be amortized in 2014 from the regulatory assets into net periodic benefit costs are $(12,000), and $(21,000), respectively.

In establishing its investment policy, our Company has considered the fact that the DB Plan is a major retirement vehicle for its employees and the basic goal underlying the establishment of the policy is to provide that the assets of the Plan are invested in accordance with the asset allocation range targets to achieve our expected return on Plan assets. Our Company's investment strategy applies to its OPEB Plans as well as the DB Plan. Our expected long-term rate of return on DB Plan and OPEB Plan assets is based on the Plans' expected asset allocation, expected returns on various classes of Plan assets as well as historical returns.

The assets of our Post-65 Plan are held in two separate Voluntary Employee Beneficiary Association ("VEBA") trusts. We maintain our VEBA plan assets in directed trust accounts at a commercial bank.

The investment strategy for our DB Plan and our OPEB Plans utilizes several different asset classes with varying risk/return characteristics. The following table indicates the asset allocation percentages of the fair value of the DB Plan and OPEB Plans' assets for each major type of plan asset as of December 31, 2013, as well as the targeted allocation range:

	DB Plan		OPEB Plans	
		Asset Allocation Range		Asset Allocation Range
Equities	64%	30% - 100%	70%	30% - 100%
Fixed income	36%	20% - 70%	28%	0% - 50%
Cash and cash equivalents	0%	0% - 15%	2%	0% - 15%
Total	100%		100%	

The following table indicates the asset allocation percentages of the fair value of the DB Plan and OPEB Plans' assets for each major type of plan asset as of December 31, 2012, as well as the targeted allocation range:

	DB Plan		OPEB Plans	
		Asset Allocation Range		Asset Allocation Range
Equities	60%	30% - 100%	64%	30% - 100%
Fixed income	40%	20% - 70%	36%	0% - 50%
Cash and cash equivalents	0%	0% - 15%	0%	0% - 15%
Total	100%		100%	

Management uses its best judgment in estimating the fair value of its financial instruments. However, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts that we could have realized in a sales transaction for these instruments. The estimated fair value amounts have been measured as of year-end and have not been reevaluated or updated for purposes of these financial statements subsequent to those respective dates.

Investments in mutual funds are stated at fair value by reference to quoted market prices. Money market funds are valued utilizing the Net Asset Value per unit based on the fair value of the underlying assets as determined by the directed trustee.

The DB Plan also holds assets under an immediate participation guarantee group annuity contract with a life insurance company. The assets under the contract are invested in pooled separate accounts and in a general investment account. The pooled separate accounts are valued based on net asset value per unit of participation in the fund and have no unfunded commitments or significant redemption restrictions at year-end. The value of these units is determined by the trustee based on the current market values of the underlying assets of the pooled separate accounts. Therefore, the value of the pooled separate accounts is deemed to be at estimated fair value.

The general investment account is not actively traded and significant other observable inputs are not available. The fair value of the general investment account is calculated by discounting the related cash flows based on current yields of similar instruments with comparable durations.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Plan's management believes the valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain investments could result in a different fair value measurement at the reporting date.

We use a fair value hierarchy which prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

The fair value of DB Plan and OPEB Plan assets by levels within the fair value hierarchy used as of December 31, 2013 was as follows:

(in thousands)	Totals	Level 1	Level 2	Level 3
DB Plan:				
Equities:				
Pooled separate accounts	$ 7,895	$ -	$ 7,895	$ -
Fixed Income:				
General investment account	2,940	-	-	2,940
Pooled separate accounts	1,409	-	1,409	-
Total Pension Plan	$ 12,244	$ -	$ 9,304	$ 2,940
OPEB Plans:				
Mutual funds:				
Balanced/hybrid funds	$ 168	$ 168	$ -	$ -
U.S. equity securities funds	416	416	-	-
International equity funds	76	76	-	-
Fixed income funds	261	261	-	-
Cash and cash equivalents:				
Money market funds	23	-	23	-
Total Post-retirement Plans	$ 944	$ 921	$ 23	$ -
Totals	$ 13,188	$ 921	$ 9,327	$ 2,940

The fair value of DB Plan and OPEB Plan assets by levels within the fair value hierarchy used as of December 31, 2012 was as follows:

(in thousands)	Totals	Level 1	Level 2	Level 3
DB Plan:				
Equities:				
Pooled separate accounts	$ 5,866	$ -	$ 5,866	$ -
Fixed Income:				
General investment account	1,704	-	-	1,704
Pooled separate accounts	2,143	-	2,143	-
Total Pension Plan	$ 9,713	$ -	$ 8,009	$ 1,704
OPEB Plans:				
Mutual funds:				
Balanced/hybrid funds	$ 179	$ 179	$ -	$ -
U.S. equity securities funds	274	274	-	-
International equity funds	67	67	-	-
Fixed income funds	297	297	-	-
Cash and cash equivalents:				
Money market funds	1	-	1	-
Total Post-retirement Plans	$ 818	$ 817	$ 1	$ -
Totals	$ 10,531	$ 817	$ 8,010	$ 1,704

Level 1: Based on quoted prices in active markets for identical assets.
Level 2: Based on significant observable inputs.
Level 3: Based on significant unobservable inputs.

The following table presents a period-end reconciliation of DB Plan assets measured and recorded at fair value on a recurring basis, using significant unobservable inputs (level 3):

(in thousands)	2013	2012
Balance, beginning of year	$ 1,704	$ 1,735
Plan transfers	864	285
Contributions	729	-
Benefits paid	(410)	(369)
Return on plan assets (net of investment expenses)	53	53
Balance, end of year	$ 2,940	$ 1,704

In order to satisfy the minimum funding requirements of the Employee Retirement Income Security Act of 1974, applicable to defined benefit pension plans, we anticipate that we will contribute approximately $1.2 million to the DB Plan in 2014.

The following maximum benefit payments, which reflect expected future service, as appropriate, are expected to be paid in the years indicated:

(in thousands)	DB Plan	OPEB Plans
2014	$ 543	$ 68
2015	599	76
2016	686	84
2017	743	96
2018	827	116
2019 - 2023	5,553	740
Total	$ 8,951	$ 1,180

Because we are subject to regulation in the state in which we operate, we are required to maintain our accounts in accordance with the regulatory authority's rules and regulations. In those instances, we follow the guidance of ASC 980 ("Regulated Operations"). Based on prior regulatory practice, we recorded underfunded DB Plan and OPEB Plan obligations as a regulatory asset and we expect to recover those costs in rates charged to customers.

Defined Contribution Plan

In addition to the defined benefit plan, we have a defined contribution plan covering substantially all employees. Under this plan, our Company matches 100% of the first 3% of each participating employee's salary contributed to the plan. The matching employer's contributions, recorded as operating expenses, were approximately $197,000 and $205,000 for the years ended December 31, 2013 and 2012, respectively.

Note 6 - Commitments and Contingencies

Operating Leases

We lease our corporate office space as well as certain office equipment under operating lease agreements. Total rent expense was approximately $305,000 and $314,000 for the years ended December 31, 2013 and 2012, respectively.

Our remaining non-cancelable lease commitments for our corporate office space and leased equipment as of December 31, 2013 were as follows:

(in thousands)	Amount
2014	$ 286
2015	269
2016	269
2017	157
2018	-
Total	$ 981

Note 7 – Financial Measurement and Fair Value of Financial Instruments

Management uses its best judgment in estimating the fair value of its financial instruments. However, there are inherent weaknesses in any estimation technique. Therefore, for substantially all financial instruments, the fair value estimates herein are not necessarily indicative of the amounts that we could have realized in a sales transaction for these instruments. The estimated fair value amounts have been measured as of the period end and have not been reevaluated or updated for purposes of these financial statements subsequent to those respective dates.

We use a fair value hierarchy which prioritizes the inputs to valuation methods used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of fair value hierarchy are as follows:

Level 1: Based on quoted prices in active markets for identical assets.

Level 2: Based on significant observable inputs.

Level 3: Based on significant unobservable inputs.

An asset or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

For assets and liabilities measured at fair value on a recurring basis, the fair value measurement by levels within the fair value hierarchy used as of December 31, 2013 and 2012 were as follows:

	December 31, 2013			
(in thousands)	Total	Level 1	Level 2	Level 3
Interest rate swap	$ (386)	$ -	$ (386)	$ -

	December 31, 2012			
(in thousands)	Total	Level 1	Level 2	Level 3
Interest rate swap	$ (825)	$ -	$ (825)	$ -

The carrying value of certain financial instruments included in the accompanying Consolidated Balance Sheets, along with the related fair value, as of December 31, 2013 and 2012 was as follows:

	2013		2012	
(in thousands)	Carrying Value	Fair Value	Carrying Value	Fair Value
Liabilities:				
Long-term debt	$ (177,396)	$ (197,797)	$ (177,058)	$ (189,149)
Interest rate swap liability	(386)	(386)	(825)	(825)

The fair value of long-term debt has been determined by discounting the future cash flows using current market interest rates for similar financial instruments of the same duration. The fair value for long-term debt shown above does not purport to represent the amounts at which those debt obligations would be settled. The fair market value of our interest rate swap represents the estimated cost to terminate this agreement as of December 31, 2013 and 2012 based upon the then-current interest rates and the related credit risk.

The carrying values of our Cash and Cash Equivalents, Accounts Receivable and Accounts Payable approximate their fair values because of their short maturity dates. The carrying value of our CIAC approximates its fair value because it is expected that this is the amount that will be recovered in future rates.

Note 8 – Income Taxes

The components of the federal and state income tax provision (benefit) as of December 31, 2013 and 2012 were as follows:

(in thousands)	2013	2012
Federal	$ (623)	$ (507)
State	(192)	(137)
Amortization of investment tax credits	(33)	(36)
Total	$ (848)	$ (680)
Current	$ -	$ (1,255)
Deferred	(848)	575
Total	$ (848)	$ (680)

The following is a reconciliation between the statutory federal income tax rate and the effective income tax rate for 2013 and 2012:

	2013	2012
Statutory federal rate	34.0%	34.0%
State tax rate, net of federal benefits	5.6%	5.5%
Permanent differences	5.6%	-14.6%
Amortization of investment tax credits	1.8%	1.4%
Effective tax rate	47.0%	26.3%

The temporary items that give rise to the net deferred tax liability as of December 31, 2013 and 2012 were as follows:

(in thousands)	2013	2012
Liabilities:		
Property-related, net	$ 24,735	$ 24,834
Pension deferred asset	1,511	3,119
Other	705	1,426
Total liabilities	26,951	29,379
Assets:		
Pension accrued liability	2,082	3,508
Federal net operating loss carryforward	2,053	1,858
Alternative minimum tax credit	384	240
NH Business Enterprise Tax credits	250	23
Other	2,375	3,125
Total assets	7,144	8,754
Net non-current deferred income tax liability	$ 19,807	$ 20,625

We had a federal net operating loss in 2013 and 2012 in the amounts of approximately $319,000 and $4.1 million, respectively. The federal tax benefit of the cumulative net operating loss is approximately $1.6 million which begins to expire in 2032, and is included in deferred income taxes in the consolidated balance sheet as of December 31, 2013.

As of December 31, 2013 and 2012, we estimated approximately $384,000 and $240,000 of cumulative federal alternative minimum tax credits that may be carried forward indefinitely as a credit against our regular tax liability.

As of December 31, 2013 and 2012, we had New Hampshire Business Enterprise Tax ("NHBET") credits of approximately $250,000 and $23,000, respectively. NHBET credits begin to expire in 2017. We anticipate that we will fully utilize these NHBET credits before they expire; therefore we have not recorded a valuation allowance related to these credits.

Investment tax credits resulting from utility plant additions are deferred and amortized. The unamortized investment tax credits are being amortized through the year 2033.

We had a regulatory liability related to income taxes of approximately $825,000 and $846,000 as of December 31, 2013 and 2012, respectively. This represents the estimated future reduction in revenues associated with deferred taxes which were collected at rates higher than the currently enacted rates and the amortization of deferred investment tax credits.

We made a review of our portfolio of uncertain tax positions. In this regard, an uncertain tax position represents our expected treatment of a tax position taken in a filed tax return, or planned to be taken in a future tax return, that has not been reflected in measuring income tax expense for financial reporting purposes. As a result of this review, we determined that we had no material uncertain tax positions. We will use tax planning strategies, if required, and when possible, to avoid the expiration of any future net operating loss and/or tax credits.

We file income tax returns in the U.S. federal jurisdiction, the State of New Hampshire and the Commonwealth of Massachusetts. Our 2010 through 2012 tax years remain subject to examination by the Internal Revenue Service. Our tax year 2009 was audited by the Internal Revenue Service and the year was closed with no changes. Our 2008 through 2012 tax years remain subject to examination by one or more state jurisdictions.

Our practice is to recognize interest and/or penalties related to income tax matters in "Other, Net" in the Consolidated Statements of Income. We incurred no interest or penalties during the year ended December 31, 2013.

Note 9 – Debt

Long-term debt as of December 31, 2013 and 2012 consisted of the following:

(in thousands)	2013	2012
Unsecured note payable to City of Nashua, 5.75%, due 12/25/2041	$ 116,336	$ 117,925
Unsecured senior note payable due to an insurance company 7.40%, due March 1, 2021	5,200	5,600
Unsecured Business Finance Authority:		
Revenue Bond (2005 Series BC-4), 5.375%, due October 1, 2035	12,125	12,130
Revenue Bond (2005 Series BC-3), 5.00%, due April 1, 2018	7,475	7,475
Revenue Bond (2005 Series A), 4.70%, due October 1, 2035	12,125	12,125
Revenue Bond (Series 2005A), 4.70%, due January 1, 2035	1,785	1,785
Revenue Bond (Series 2005B), 4.60%, due January 1, 2030	2,320	2,320
Revenue Bond (Series 2005C), 4.50%, due January 1, 2025	1,175	1,175
Revenue Bond, 1997, 6.30%, due May 1, 2022	2,800	3,000
Unsecured notes payable to bank, floating-rate, due March 1, 2030	3,886	4,058
Unsecured notes payable to bank, 3.62%, due June 20, 2023	1,694	-
Unsecured notes payable to bank, 4.25%, due June 20, 2033	910	-
Unsecured New Hampshire State Revolving Fund ("SRF") notes (1)	9,829	9,741
Total long-term debt	177,660	177,334
Less current portion	(2,965)	(2,780)
Less original issue discount	(264)	(275)
Total long-term debt, net of current portion	$ 174,431	$ 174,279

(1) SRF notes are due through 2033 at interest rates ranging from 1% to 4.488%. These notes are payable in 120 to 240 consecutive monthly installments of principal and interest. The 1% rate applies to construction projects still in process until the earlier of (i) the date of substantial completion of the improvements, or (ii) various dates specified in the note (such earlier date being the interest rate change date). Commencing on the interest rate change date, the interest rate changes to the lower of (i) the rate as stated in the note or (ii) 80% of the established 11 General Obligations Bond Index published during the specified time period before the interest rate change date.

The aggregate principal payment requirements subsequent to December 31, 2013 are as follows:

(in thousands)	Amount
2014	$ 2,965
2015	3,108
2016	3,242
2017	3,384
2018	11,008
2019 and thereafter	153,953
Total	$ 177,660

Several of Pennichuck Water's loan agreements contain a covenant that prevents Pennichuck Water from declaring dividends if Pennichuck Water does not maintain a minimum net worth of $4.5 million. As of December 31, 2013 and 2012, Pennichuck Water's net worth was $125.6 and $130.9 million, respectively. Pennichuck Water Works also has debt issuance covenants whereby they must also maintain a maximum total debt to capital ratio of 65%, a maximum funded debt to net property, plant and equipment ratio of 60%, and an interest coverage ratio of at least 1.5; at December 31, 2013 and 2012 the total debt to capital ratio was 29% and 28%, respectively, the funded debt to net property, plant and equipment ratio was 38% and 39%, respectively, and the interest coverage ratio was 2.62 and 3.17.

Pennichuck East's loan agreement for its unsecured notes payable to a bank of $3.9 million and $4.1 million at December 31, 2013 and 2012, respectively, contains a minimum debt service coverage ratio requirement of 1.25. At December 31, 2013 and 2012 this ratio was 1.42 and 1.69, respectively. Also, Pennichuck East is required to maintain a maximum ratio of total debt to total capitalization of 65%; at December 31, 2013 and 2012 this ratio was 41% and 34%, respectively.

The Company's revolving credit loan facility with RBS Citizens contains a covenant that requires the Company to maintain a minimum fixed charge coverage ratio of at least 1.0; at December 31, 2013 and 2012 the fixed charge coverage ratio was 1.08 and 1.25, respectively. The Company is also required to maintain an equity capitalization ratio of not less than 35%; at December 31, 2013 and 2012, the equity capitalization ratio was 50% and 52%, respectively. Under this agreement the Company is also precluded from declaring or paying dividends, or making any other payment or distribution of its equity without the bank's prior written consent, except for: (1) its obligations under Rate Order No. 25,292 as it pertains to the Company's specific obligations under the City Bond Fixed Revenue Requirement ("CBFRR") which provides for payments of approximately $707,000 per month of the note payable to the City of Nashua (the "City"), and quarterly dividends to the City for the remainder of this annual obligation, as defined by the order; and (2) a specific allowance, under Rate Order No. 25,292, whereby the Company is allowed to make distributions to the City from current earnings and profits in excess of the CBFRR, to provide funds to allow the City to reimburse itself for the costs incurred by the City relating to its efforts in pursuing the eminent domain proceedings from January 2002 through August 2009, provided however that such amount shall not exceed $500,000 in any fiscal year, or

$5,000,000 in the aggregate, of all such distributions. During the year ended December 31, 2013, a special dividend was approved and paid relating to this.

Our short-term borrowing activity under this revolving credit loan facility for the years ended December 31, 2013 and 2012 was:

(in thousands)	2013	2012
Established line as of December 31,	$ 10,000	$ 10,000
Maximum amount outstanding during period	1,966	-
Average amount outstanding during period	137	-
Amount outstanding as of December 31,	1,966	-
Weighted average interest rate during period	1.06%	n/a
Interest rate as of December 31,	2.665%	n/a

As of December 31, 2013 and 2012, we had a $3.9 million and $4.1 million, respectively, interest rate swap which qualifies as a derivative. This financial derivative is designated as a cash flow hedge. This financial instrument is used to mitigate interest rate risk associated with our outstanding $4.1 million loan which has a floating interest rate based on the three-month London Interbank Offered Rate ("LIBOR") plus 1.75% as of December 31, 2013. The combined effect of the LIBOR-based borrowing formula and the swap produces an "all-in fixed borrowing cost" equal to 5.95%. The fair value of the financial derivative, as of December 31, 2013 and 2012, included in our Consolidated Balance Sheets under "Deferred credits and other reserves" as "Other liabilities" was $386,000 and $825,000, respectively. Changes in the fair value of this derivative were deferred in accumulated other comprehensive loss.

Swap settlements are recorded in the statement of income with the hedged item as interest expense. During the years ended December 31, 2013 and 2012 $156,000 and $157,000 was reclassified pre-tax from accumulated other comprehensive loss to interest expense as a result of swap settlements. We expect to reclassify approximately $150,000, pre-tax, from accumulated other comprehensive loss to interest expense as a result of swap settlements, over the next twelve months.

Note 10 – Transaction with the City of Nashua

On January 25, 2012, in full settlement of an ongoing Eminent Domain lawsuit filed by the City of Nashua ("City") and with the approval of the New Hampshire Public Utilities Commission ("NHPUC"), the City acquired all of the outstanding shares of Pennichuck Corporation ("Pennichuck") and, thereby, indirect acquisition of its regulated subsidiaries. The total amount of the acquisition was $150.6 million ("Acquisition Price") of which $138.4 million was for the purchase of the outstanding shares, $5.0 million for the establishment of a Rate Stabilization Fund, $2.6 million for legal and due diligence costs, $2.3 million for severance costs, $1.3 million for underwriting fees, and $1.0 million for bond discount and issue costs. The entire purchase of $150.6 million was funded by General Obligation Bonds ("Bonds") issued by the City of Nashua. Pennichuck is not a party to the Bonds and has not guaranteed nor is obligated in any manner for the repayment of the Bonds. Pennichuck remains an independent corporation with an independent Board of Directors with the City of Nashua as its sole shareholder.

Pennichuck Water Works, Inc. ("PWW"), Pennichuck East Utility, Inc. ("PEU"), Pittsfield Aqueduct Company, Inc. ("PAC"), Pennichuck Water Service Corporation, and The Southwood Corporation will continue as subsidiaries of Pennichuck Corporation and PWW, PEU and PAC will continue as regulated companies under the jurisdiction of the New Hampshire Public Utilities Commission. The terms of the merger and the requisite accounting and rate-setting mechanisms were agreed to in the NHPUC Order 25,292 ("PUC Order") dated November 23, 2011.

Transactions with Related Party – City of Nashua

Pennichuck issued a promissory note to the City of Nashua in the amount of approximately $120 million to be repaid over a thirty (30) year period with monthly payments of approximately $707,000, including interest at 5.75%. Pennichuck recorded an additional amount of approximately $30.6 million as contributed capital. The remaining outstanding balance of the note payable to the City at December 31, 2013 and December 31, 2012 was approximately $116.3 million and $117.9 million, respectively, as disclosed in Note 9 to these consolidated financial statements. During 2013 and 2012, dividends of approximately $777,000 and $210,000, respectively, were declared and paid to the City. The dividends paid to the City during 2013 comprised approximately $277,000 of regular quarterly dividends declared and paid, and a special dividend of $500,000 declared and paid in October 2013, as resolved and authorized by the Board of Directors in their August 23, 2013 meeting.

Additional ongoing transactions occur in the normal course of business, between the Company and the City, related to municipal water usage, fire protection and sewer billing support services, and property taxes related to real property owned by the Company within the City of Nashua. For the years ended December 31, 2013 and 2012, respectively, approximately $3.1 million and $3.0 million were paid to the Company by the City for municipal water consumption, fire protection charges, and sewer billing support services. Conversely, the Company paid property taxes to the City of Nashua of approximately $2.4 million for the year ended December 31, 2013, and approximately $2.1 million for the year ended December 31, 2012.

Rate Stabilization Fund – Restricted Cash

As a part of the acquisition, Pennichuck agreed to contribute $5,000,000 of the proceeds from the settlement transaction to PWW, which was used to establish a Rate Stabilization Fund ("RSF"), allowing for the maintenance of stable water utility rates and providing a mechanism to ensure the Company's continued ability to meet its obligations under the promissory note to the City, in the event of adverse revenue developments. Restricted cash consists of amounts set aside in the RSF account, and is adjusted monthly as required in the PUC Order, as discussed in Note 1 of these financial statements.

Municipal Acquisition Regulatory Asset ("MARA")

Pursuant to the PUC Order, Pennichuck established a new Regulatory asset (MARA) which represents the amount that the Acquisition Price exceeded the net book assets of Pennichuck's regulated subsidiaries (PWW, PEU, and PAC) at December 31, 2011. The initial amount of the MARA was approximately $89 million for the regulated companies, offset by a non-regulated amount of approximately $4.8 million. The MARA is to be amortized over a thirty (30) year period in the same manner as the repayment of debt service for the City's acquisition bonds. The balance in the MARA at December 31, 2013 was approximately $85.4 million, reduced by the non-regulated credit of approximately $4.7 million.

Aggregate amortization expense for the years ended December 31, 2013 and 2012, totaled approximately $2,542,000 and $1,023,000, respectively. During the year ended December 31, 2012, the amortization of the MARA was calculated based upon the amortization of principal for the Company's unsecured note payable to the City of Nashua (see Note 9). However, during 2013 the Company realized that the amortization of the MARA, as authorized by NHPUC Order 25,292, dated November 23, 2011, was supposed to be calculated based upon the principal repayment schedule of the bonds issued by the City, in support of their acquisition of the Company in January 2012. As such, the Company made a one-time adjustment to "true up" the amortization of the MARA during 2013, and as such, approximately $716,000 of the amortization expense recorded in 2013 relates to amounts that would have been booked in 2012, had the correct basis been applied initially. The amortization amounts for 2013 and 2012, respectively, would have been approximately $1,826,000 and $1,739,000 for each of the years, after giving consideration for this one-time correction.

The following table represents the total estimated amortization of MARA for the five succeeding years:

(in thousands)	Estimated Amortization Expense
2014	$ (1,834)
2015	(1,857)
2016	(1,884)
2017	(1,917)
2018	(1,958)

Note 11 – Sale of Land

On January 24, 2012, Southwood sold a 38-acre parcel of undeveloped land for approximately $2.2 million. The resulting net gain from this transaction of approximately $1.6 million, is included in gain on sale of land on the accompanying consolidated statement of income.

Note 12 – Sale of Conservation Easement

In July 2013, the Company completed the sale of a conservation easement to the Society for the Protection of New Hampshire Forests, with respect to a portion of its non-regulated land holdings in Merrimack, New Hampshire, as approved by the Board of Directors in their April 26, 2013 meeting. The transaction included gross proceeds for the value of the easement of approximately $991,000, netted by approximately $100,000 of legal, surveying, and professional fees. The net proceeds of approximately $891,000 from this transaction are included in "Other, Net" on the Consolidated Statements of Income herein.

Note 13 – Subsequent Events

The Company has evaluated the events and transactions that have occurred through March 19, 2014, the date that these financial statements were available for issuance, and noted no items requiring an adjustment to the financial statements or additional disclosure.