

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program**

Independent Auditor's Report and Financial Statements

June 30, 2015 and 2014



# State of Arkansas Construction Assistance Revolving Loan Fund Program

June 30, 2015 and 2014

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## Independent Auditor's Report

The Commissioners of the Arkansas Natural  
Resources Commission (ANRC)

The Board of Directors of  
Arkansas Development Finance Authority (ADFA)

We have audited the accompanying basic financial statements of the State of Arkansas Construction Assistance Revolving Loan Fund Program (the Program), which are comprised of statements of net position as of June 30, 2015 and 2014, and the related statements of revenues, expenses and changes in net position and statements of cash flows for the years ended June 30, 2015 and 2014, and the related notes to the 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 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 financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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.

The Commissioners of the Arkansas Natural  
Resources Commission (ANRC)

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

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Program as of June 30, 2015 and 2014, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### ***Emphasis of a Matter***

As discussed in *Note 1*, the financial statements of the Program are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the business-type activities of the State of Arkansas (the State) that is attributable to the transactions of the Program. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2015 and 2014, and the changes in its financial position and its cash flows, where applicable, for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

### **Other Matters**

#### ***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis listed in the table of contents be presented to supplement the basic financial statements. Such information, although not 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.

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Resources Commission (ANRC)

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### *Supplementary Information*

Our audits were conducted for the purpose of forming an opinion on the basic financial statements as a whole. The supplementary information listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the basic financial statements as a whole.

### **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated October 29, 2015, on our consideration of the Program's internal control over financial reporting and 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 the 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 Program's internal control over financial reporting and compliance.

*BKD, LLP*

Little Rock, Arkansas  
October 29, 2015

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program  
Management's Discussion and Analysis  
June 30, 2015 and 2014**

This discussion and analysis is designed to assist the reader in focusing on significant issues and activities and to identify any significant changes in the financial position of the Construction Assistance Revolving Loan Fund Program (the Program). Readers are encouraged to consider the information presented in conjunction with the financial statements and notes as a whole, which follow this section of the report.

***Discussion of Financial Statements***

The June 30, 2015, basic financial statements include three required statements: The statement of net position; the statement of revenues, expenses and changes in net position; and the statement of cash flows. Comparative totals as of and for the years ended June 30, 2014 and 2013, are also presented. Although not required, these comparative totals are intended to facilitate an enhanced understanding of the Program's financial position and results of operations for the current fiscal year in comparison to the prior fiscal years. Additional information, following the *Notes to Financial Statements*, includes the combining statement of net position; the combining statement of revenues, expenses and changes in net position; as well as the combining statement of cash flows. These combining statements detail the Revolving Loan Fund and the Fees and Expenses Fund, which comprise the Program.

***Condensed Financial Information – Statements of Net Position***

<i>(In thousands)</i>	<u>2015</u>	<u>2014</u>	<u>2013</u>
Total assets and deferred outflow of resources	\$ <u>387,347</u>	\$ <u>384,220</u>	\$ <u>385,221</u>
Current liabilities	4,317	5,288	11,501
Noncurrent liabilities	<u>34,537</u>	<u>39,175</u>	<u>45,607</u>
Total liabilities	<u>38,854</u>	<u>44,463</u>	<u>57,108</u>
Net position – restricted by bond resolution and program requirements	\$ <u>348,493</u>	\$ <u>339,757</u>	\$ <u>328,113</u>

The Program's total assets and deferred outflow of resources have fluctuated over the past three years. At June 30, 2015, the total assets increased \$3.1 million compared to June 30, 2014, which was primarily attributed to an increase of \$38.2 million in cash and cash equivalents and investments – current portion, which was offset by a decline in loan receivable - restricted of \$34.8 million. At June 30, 2014, the balance of \$384.2 declined \$1.0 million compared to June 30, 2013, which was attributed to a decrease in cash and cash equivalents and investments of \$8.8 million, which is offset by an increase of \$7.8 million in loans receivable. The following table reports loan activity for each year (in thousands):

**State of Arkansas Construction Assistance  
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	<u>2015</u>	<u>2014</u>	<u>2013</u>
Loan disbursements	\$ 23,776	\$ 41,007	\$ 60,729
Loan repayments	<u>58,596</u>	<u>33,255</u>	<u>29,838</u>
Net (decrease) increase in loans receivable	\$ <u>(34,820)</u>	\$ <u>7,752</u>	\$ <u>30,891</u>

The following table reflects the disbursement of funds to new and existing loan borrowers (in thousands):

	<u>2015</u>	<u>2014</u>	<u>2013</u>
New loans	\$ 10,350	\$ 13,500	\$ 66,000
Loan disbursements – new loans	1,030	7,009	4,171
Existing loans	79,500	156,000	130,300
Loan disbursements – existing loans	22,746	33,998	56,558

The Program continually made loans from federal grant funds from Environmental Protection Agency (EPA), prepayment funds, state matching funds and revolving Program funds. The Program received federal funds in the form of an annual capitalization grant (Base). Currently, the Program is experiencing a decline in the number of requests from municipalities for assistance in maintaining their water and sewer systems. In the current fiscal year, the Program focused mainly on using the revolving Program funds and state match funds. The Program matches federal grant awards prior to receiving the federal grant at a rate of five federal dollars to one state dollar. In the current fiscal year, the Program matched \$2.8 million and disbursed \$2.5 million relating to the 2014 and 2015 federal capitalization grant. The Program received loan prepayments totaling \$43.5 million. The Program's general bond resolution allows prepayment funds to be used to make new loans within 90 days of receipt, pay principal and interest at debt service or pay principal and interest on called bonds. In the prior fiscal year, the Program utilized the prepayment funds and the revolving Program funds to make loan disbursements while still utilizing the EPA Base federal grants funds available. The table below reflects the amounts used from each funding source for fiscal years 2015, 2014 and 2013 (in thousands):

	<u>2015</u>	<u>2014</u>	<u>2013</u>
EPA Federal			
Base	\$ 1,886	\$ 5,714	\$ 14,724
State Matching	2,519	728	4,181
2009 Issue Prepayment Funds	6,468	13,105	2,986
Revolving Program Funds	<u>12,903</u>	<u>21,460</u>	<u>38,838</u>
	\$ <u>23,776</u>	\$ <u>41,007</u>	\$ <u>60,729</u>

The Program utilized its cash within the Program as an additional funding source, essentially revolving the assets.

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The Federal fiscal year 2015 Base grant has been approved by the EPA in the amount of \$9.1 million and will be available in October 2015.

The Program's total liabilities decreased to \$38.9 million at June 30, 2015, from \$44.5 million at June 30, 2014, and from \$57.1 million at June 30, 2013. The decline of \$5.6 million and \$12.6 million for fiscal years 2015 and 2014, respectively, was attributable to the scheduled bond redemptions.

**Condensed Financial Information – Statements of Revenues, Expenses and Changes in Net Position**

*(In thousands)*

	2015	2014	2013
Total interest income	\$ 5,502	\$ 5,574	\$ 5,291
Other income	<u>2,111</u>	<u>2,526</u>	<u>2,666</u>
Total operating revenues	<u>7,613</u>	<u>8,100</u>	<u>7,957</u>
Total interest on bonds and notes	1,803	2,222	3,610
Total amortization expense	(638)	(933)	(932)
Federal financial assistance	116	1,630	612
Administrative expense	<u>239</u>	<u>250</u>	<u>251</u>
Total operating expenses	<u>1,520</u>	<u>3,169</u>	<u>3,541</u>
Operating income	6,093	4,931	4,416
Base federal grants	2,323	7,693	15,706
ARRA federal grants	-	-	1
Transfers in (out), net	<u>320</u>	<u>(980)</u>	<u>(1,080)</u>
Change in net position	8,736	11,644	19,043
Net position			
Beginning of year	<u>339,757</u>	<u>328,113</u>	<u>309,070</u>
End of year	<u>\$ 348,493</u>	<u>\$ 339,757</u>	<u>\$ 328,113</u>



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Total operating revenues has fluctuated over the past three years. Operating revenues decreased \$487,000 during fiscal year 2015 and increased \$143,000 during fiscal year 2014. In the current fiscal year, the Program's interest income on loans, net depreciation of investments and financing fee income decreased \$822,000, which was offset by an increase in the interest income on investments of \$335,000. The decrease in interest income on loans and financing fee income correlated to the decrease in loans receivable – restricted. The Program received \$43.5 million in loan prepayments in the current fiscal year. In the prior fiscal year, the Program's interest income from loans, net depreciation of investments and financing fee income increased \$648,000, which was offset by the decreases in other income of \$435,000 and interest income on investments of \$70,000. In the prior fiscal year, the Program's interest income from loans and financing fee income increased due to the continuous funding of loans which correlated to the increase in loan receivable – restricted. Overall, the Program has a return on loan interest income of 2.22%, 2.08% and 2.12% for fiscal years 2015, 2014 and 2013, respectively.

Revenues from investments were \$483,000, \$148,000 and \$218,000 for fiscal years ended June 30, 2015, 2014 and 2013, respectively. The average return on cash, cash equivalents and investments was 0.05%, 0.07% and 0.09% for years ended June 30, 2015, 2014 and 2013, respectively. The Program maintains liquidity to fund projects as needed. The Program invested excess funds in U. S. agencies obligations at higher yields than current money market mutual fund rates.

Base federal grants revenue decreased \$5.4 million in the current fiscal year. The Base federal grants guidelines allow for the funding of forgiveness of principal and repayable loans. The Program has \$8.8 million of the Federal Fiscal Year 2014 grant to expend for loans. For the prior fiscal year, the Program had \$2.0 million of the Federal Fiscal Year 2013 grant still to expend for loans. Information regarding when Base federal grant awards were expended for construction draws and principal forgiveness loans is as follows (in thousands):

Federal Award Year	Beginning Balance	Amount Expended in		
		FY2013	FY2014	FY2015
2010	\$ 10,168	\$ 2,611	\$ -	\$ -
2011	9,272	4,468	360	-
2012	8,869	8,256	613	-
2013	8,373	-	6,371	2,002
2014	8,798	-	-	-
		<u>\$ 15,335</u>	<u>\$ 7,344</u>	<u>\$ 2,002</u>

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The Program continues to fund loans from other revenue sources including \$21.9 million from the Program funds, state match funds and loan prepayments.

Operating expenses decreased by \$1.7 million and \$372,000 during 2015 and 2014, respectively. During fiscal years 2015 and 2014, the Program forgave principal of \$116,000 and \$1.6 million, respectively. In the fiscal year 2013, the Program began making principal forgiveness loans from the Base capitalization grants per EPA requirements. The Program's interest on bonds and notes decreased \$419,000 and \$1.4 million during fiscal years 2015 and 2014, respectively, which correlated to the decrease in bonds payable. Program administration expenses totaled \$239,000, \$250,000 and \$251,000 for the fiscal years ended June 30, 2015, 2014 and 2013, respectively. These expenses included amounts paid for audit expense, trustee fees and the administrative fee to the Arkansas Development Finance Authority (ADFA).

Transfers in and out are comprised of transfers to or from other state programs or agencies. In the current fiscal year, the Program received transfers in of \$1 million from the Arkansas Natural Resources Commission (ANRC) Water, Waste Disposal and Pollution Abatement Facilities General Obligation Bond Fund Program to fund state match, which is offset by transfers out of \$680,000 to ANRC for administrative expenses of the Program. In the prior fiscal year, the Program transferred out \$980,000 to ANRC for administrative expenses of the Program. The funding source for the administrative expenses is 4% of the EPA capitalization grant along with funds from the Fees and Expenses Fund.

The net position of the Program increased \$20.4 million in the past two years. The bond resolutions and the Program restrict all of the net position.

The overall financial position and results of operations of the Program have improved.

***Contact Regarding the Program***

This financial report is designed to provide bondholders, constituents and business partners with a general overview of the Program's finances and to show the Program's accountability for the funds it administers. Questions about this report and requests for additional financial information should be directed to the ADFA Vice President for Finance and Administration by telephoning 501.682.5900 or by contacting the ANRC Water Development Division Chief at 501.682.1611.

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Statements of Net Position June 30, 2015 and 2014

(In thousands)

	2015	2014
<b>Current Assets</b>		
Cash and cash equivalents	\$ 101,162	\$ 82,850
Accrued interest receivable		
Investments	154	16
Loans	258	528
Accounts receivable		
Borrowers	154	256
Environmental Protection Agency	-	15
Investments – current portion	59,715	39,815
Total current assets	161,443	123,480
<b>Noncurrent Assets</b>		
Loans receivable – restricted		
Construction	224,951	259,771
Wetlands mitigation	933	933
Total noncurrent assets	225,884	260,704
Total assets	387,327	384,184
<b>Deferred Outflow of Resources</b>		
Deferred charge on refunding	20	36
<b>Current Liabilities</b>		
Accounts payable	184	213
Accrued interest payable	133	150
Bonds payable – current portion	4,000	4,925
Total current liabilities	4,317	5,288
<b>Noncurrent Liabilities</b>		
Bonds payable, net of unamortized premiums	34,537	39,175
Total liabilities	38,854	44,463
<b>Net Position</b>		
Restricted by bond resolution and program requirements	\$ 348,493	\$ 339,757

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**Years Ended June 30, 2015 and 2014**

(In thousands)

	2015	2014
<b>Operating Revenues</b>		
Interest on investments	\$ 483	\$ 148
Interest on loans	5,019	5,426
Financing fees	2,545	2,602
Net depreciation of investments	<u>(434)</u>	<u>(76)</u>
Total operating revenues	<u>7,613</u>	<u>8,100</u>
<b>Operating Expenses</b>		
Program administration	239	250
Federal financial assistance		
Base	116	1,630
Bond interest	1,803	2,222
Amortization of bond premiums	<u>(638)</u>	<u>(933)</u>
Total operating expenses	<u>1,520</u>	<u>3,169</u>
<b>Operating Income</b>	<u>6,093</u>	<u>4,931</u>
<b>Nonoperating Revenues</b>		
Base federal grants	<u>2,323</u>	<u>7,693</u>
Total nonoperating revenues	<u>2,323</u>	<u>7,693</u>
<b>Income Before Transfers In (Out), Net</b>	8,416	12,624
<b>Transfers In (Out), Net</b>	<u>320</u>	<u>(980)</u>
<b>Change in Net Position</b>	8,736	11,644
<b>Net Position, Beginning of Year</b>	<u>339,757</u>	<u>328,113</u>
<b>Net Position, End of Year</b>	<u>\$ 348,493</u>	<u>\$ 339,757</u>

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Statements of Cash Flows Years Ended June 30, 2015 and 2014

(In thousands)

	2015	2014
<b>Operating Activities</b>		
Interest received on investments	\$ 345	\$ 191
Interest received on loans	5,289	5,377
Financing fee income received	2,647	2,570
Loan disbursements	(23,776)	(41,007)
Principal repayments on loans	58,596	33,255
Cash paid for interest	(1,804)	(2,232)
Federal grant funds expended	(116)	(1,630)
Cash paid for program administration	<u>(268)</u>	<u>(241)</u>
Net cash provided by (used in) operating activities	<u>40,913</u>	<u>(3,717)</u>
<b>Noncapital Financing Activities</b>		
Repayment of long-term debt	(4,925)	(11,685)
Transfers in (out)	320	(980)
Nonoperating grants received	<u>2,338</u>	<u>7,679</u>
Net cash used in noncapital financing activities	<u>(2,267)</u>	<u>(4,986)</u>
<b>Investing Activities</b>		
Proceeds from maturities of investments	66,997	38,569
Purchase of investments	<u>(87,331)</u>	<u>(40,104)</u>
Net cash used in investing activities	<u>(20,334)</u>	<u>(1,535)</u>
<b>Increase (Decrease) in Cash and Cash Equivalents</b>	18,312	(10,238)
<b>Cash and Cash Equivalents, Beginning of Year</b>	<u>82,850</u>	<u>93,088</u>
<b>Cash and Cash Equivalents, End of Year</b>	<u>\$ 101,162</u>	<u>\$ 82,850</u>

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program  
Statements of Cash Flows (Continued)  
Years Ended June 30, 2015 and 2014**

(In thousands)

	<b>2015</b>	<b>2014</b>
<b>Reconciliation of Operating Income to Net Cash Provided By (Used In) Operating Activities</b>		
Operating income	\$ 6,093	\$ 4,931
Items not requiring (providing) operating activities cash flows		
Amortization of bond premiums	(638)	(933)
Amortization of deferred charge on refunding	16	27
Net depreciation of investments	434	76
Changes in		
Accrued interest receivable		
Investments	(138)	43
Loans	270	(50)
Accounts receivable – borrowers	102	(32)
Loans receivable	34,820	(7,752)
Accounts payable	(29)	10
Accrued interest payable	(17)	(37)
Net cash provided by (used in) operating activities	\$ 40,913	\$ (3,717)

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

### Note 1: Nature of Operations and Summary of Significant Accounting Policies

#### *Nature of Operations and Reporting Entity*

The State of Arkansas Construction Assistance Revolving Loan Fund Program (the Program), an enterprise fund of the State of Arkansas, was created pursuant to the 1987 Amendments (P.L.100-4) to the "Clean Water Act" (P.L.92-500) to provide a perpetual fund for financing the construction of wastewater treatment facilities for municipalities and other public entities. The Program is to be capitalized with federal grants from the U.S. Environmental Protection Agency (EPA) and state matching funds on a ratio of five federal dollars to one state dollar.

As of July 2001, Arkansas Natural Resources Commission (ANRC), formerly known as Arkansas Soil and Water Conservation Commission, became the lead agency for the Program (previously led by Arkansas Department of Environmental Quality). As lead agency, ANRC is responsible for performing technical project reviews, monitoring construction and coordinating the total management of the Program. Act 1243 of 2006 authorized the name change to ANRC, which has not had an impact on the Program. Arkansas Development Finance Authority (ADFA) serves as financial manager for the Program under an interagency agreement. ADFA is responsible for investing and disbursing funds as authorized by the lead agency, servicing loans, preparing and submitting monthly financial reports and annual financial statements and procuring audit services. ADFA is reimbursed for Program administration costs through a calculation based on loans outstanding in accordance with the interagency agreement. The amounts incurred to ADFA for administration costs for the years ended June 30, 2015 and 2014, were \$184,000 and \$206,000, respectively.

The Arkansas Agriculture Water Quality Loan Program (AAWQLP) is accounted for within the Program. Under the AAWQLP, ANRC establishes noninterest-bearing cash accounts with financial institutions. In fiscal year 2007, an agreement was established with AgriBank in which AAWQLP would purchase a noninterest bearing bond in conjunction with loans made by AgriBank under the AAWQLP guidelines. Loans are originated by the financial institution or AgriBank to the farmers or property owners that provide for the installation of water quality, anti-pollution equipment. Interest income normally earned on these balances at the financial institutions or on the bond is used to reduce the interest rates applicable to the loans obtained by the farmers or other property owners. ANRC has established a Program contribution limit to AAWQLP in the amount of \$25 million. As of June 30, 2015 and 2014, the AAWQLP had \$9.7 million and \$12.6 million, respectively, in deposits and investments with various financial institutions.

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

### ***Use of Estimates***

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of fair values of investments.

### ***Measurement Focus, Basis of Accounting and Financial Statement Presentation***

The Program is accounted for as an enterprise fund for financial reporting purposes and utilizes the economic resource measurement focus and accrual basis of accounting wherein revenues are recognized when earned and expenses when incurred.

Operating revenues and expenses are distinguished from nonoperating items in the Program's statement of revenues, expenses and changes in net position. Operating revenues and expenses generally result from providing services in connection with the principal ongoing operations. All revenues and expenses not meeting this definition are reported as nonoperating items.

### ***Cash and Cash Equivalents***

The Program considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2015 and 2014, cash equivalents of \$101.2 million and \$82.9 million, respectively, consisted primarily of money market mutual funds with variable interest rates.

Included in cash equivalents on the Program's statement of net position is the Fees and Expenses Fund with a balance of approximately \$1.9 million and \$7.7 million at June 30, 2015 and 2014, respectively. This fund contains fees charged on loans of the Program, as allowed by EPA. These funds may be used at the discretion of ANRC to fund expenses of the Program.

### ***Investments***

Investments are carried at fair value. Fair value is determined using quoted market prices.

### ***Bond Issuance Premiums***

Premiums on sales of bonds are capitalized and are amortized over the term of the bonds using the effective interest method. Early retirement of bonds results in the acceleration of amortization of premiums.



# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements June 30, 2015 and 2014

### **Financing Fees**

The Program receives a 1% monthly financing fee from borrowers.

### **Net Position Restricted by Bond Resolution and Program Requirements**

Net position restricted by bond resolution and program requirements represents funds restricted due to the specific provisions of the Program.

### **Income Taxes**

As an essential government function of the State of Arkansas, the Program is exempt from income taxes under Section 115 of the Internal Revenue Code and a similar provision of state law.

## **Note 2: Deposits and Investments**

### **Deposits**

Custodial credit risk is the risk that in the event of a bank failure, the Program's deposits may not be returned to it. The Program's deposit policy for custodial credit risk requires compliance with the provisions of state law and bond indentures. Deposits are collateralized for those amounts exceeding federal depository insurance, typically with obligations of the U.S. Treasury, U.S. agencies or instrumentalities or municipal bonds having an aggregate market value at least equal to 105% of the amount of the deposits as directed in the State Board of Finance Cash Management of Funds, Rule 2012-A.

At June 30, 2015 and 2014, \$3.0 million and \$4.5 million of the Program's deposits (and carrying value) of \$6.1 million and \$7.8 million were exposed to custodial credit risk as follows:

<i>(In thousands)</i>	<b>2015</b>	<b>2014</b>
Uninsured and collateral held by pledging financial institution trust department or agent in the Program's name	\$ <u>2,963</u>	\$ <u>4,450</u>

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

### **Investments**

Arkansas statutes and the Program's General Resolution authorizes the Program to invest in direct obligations of the U.S. government; obligations on which the principal and interest are fully guaranteed or are fully secured, insured or covered by commitments or agreements to purchase by the U.S. government; obligations of agencies and instrumentalities created by act of the United States Congress and authorized thereby to issue securities or evidence of indebtedness, regardless of guarantee of repayment by the U.S. government; obligations of political subdivisions of the United States; certain obligations issued by the State Board of Education; short-term warrants of political subdivisions of the State of Arkansas and municipalities; the sale of federal funds with a maturity of not more than one business day; demand, savings or time deposits fully insured by a federal deposit insurance agency; repurchase agreements that are fully insured by obligations of the U.S. government, any U.S. state or any political subdivision thereof; securities of, or other interest in, any open-end type investment company or investment trust registered under the Investment Company Act of 1940, and which is considered a money market fund, provided that the portfolio is limited principally to U.S. government obligations and the investment company or trust takes delivery of collateral either directly or through an authorized custodian; guaranteed investment contracts; and bank certificates of deposit.

At June 30, 2015 and 2014, the Program had the following investments and maturities:

*(In thousands)*

<u>Type</u>	<u>June 30, 2015</u>				
	<u>Fair Value</u>	<u>Maturities in Years</u>			
		<u>Less than 1</u>	<u>1-5</u>	<u>6-10</u>	<u>More than 10</u>
U.S. agencies obligations	\$ 59,714	\$ 59,714	\$ -	\$ -	\$ -
Money market mutual funds	<u>95,017</u>	<u>95,017</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 154,731</u>	<u>\$ 154,731</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

*(In thousands)*

<u>Type</u>	<u>June 30, 2014</u>				
	<u>Fair Value</u>	<u>Maturities in Years</u>			
		<u>Less than 1</u>	<u>1-5</u>	<u>6-10</u>	<u>More than 10</u>
U.S. agencies obligations	\$ 39,815	\$ 39,815	-	-	-
Money market mutual funds	<u>75,080</u>	<u>75,080</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 114,895</u>	<u>\$ 114,895</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

*Interest Rate Risk*—As a means of limiting its exposure to fair value losses due to rising interest rates, the Program’s investments typically match the term of the corresponding bonds or limits the maturity to expected cash flow needs of the Program.

*Credit Risk*—Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. The Program’s investments in U.S. agencies obligations not directly guaranteed by the U.S. government were rated “Aaa” or not rated by Moody’s Investors Service and rated AA+ or not rated by Standard & Poor’s and its investments in money market mutual funds or investments of those funds were rated “AAAm” or “AAA” by Standard & Poor’s and “Aaa-mf” or “Aaa” by Moody’s Investors Service.

*Custodial Credit Risk*—For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Program will not be able to recover the value of its investment or collateral securities that are in the possession of an outside party. The Program’s investment in mutual funds are not classified by custodial credit risk category, as they are not evidenced by securities in physical or book entry form.

*Concentration of Credit Risk*—The Program places no limit on the amount that may be invested in any one issuer. Investments of the Program (not guaranteed by the U.S. government or considered mutual funds) representing 5% or more of total investments are as follows (in thousands):

Issuer	Fair Value	Percentage
Federal Home Loan Bank	\$ 40,994	26%
FNMA	\$ 15,181	10%

### **Summary of Carrying Values**

The carrying values of deposits and investments are included in the statements of net position as follows:

<i>(In thousands)</i>	2015	2014
Carrying value		
Deposits	\$ 6,146	\$ 7,770
Investments	<u>154,731</u>	<u>114,895</u>
	<u>\$ 160,877</u>	<u>\$ 122,665</u>
Included in the following statement of net position captions		
Cash and cash equivalents	\$ 101,162	\$ 82,850
Investments – current portion	<u>59,715</u>	<u>39,815</u>
	<u>\$ 160,877</u>	<u>\$ 122,665</u>

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

### Note 3: Loans Receivable

The Program originates loans with Arkansas municipalities, sewer improvement districts, and water facilities boards for financing the construction of wastewater treatment facilities. The loans are payable in semi-annual installments. At June 30, 2015 and 2014, such loans had a carrying value of approximately \$225.9 million and \$260.7 million, respectively, of which approximately \$45.9 million and \$88.1 million, respectively, are for projects still under construction. The loans bear interest ranging from 0.00% to 3.75%, and are collateralized by special assessments, user charges or sales and use tax bonds issued by the municipalities, sewer improvement districts and water facilities board.

In fiscal year 2010, the Program began funding loans with American Recovery and Reinvestment Act (ARRA) federal funds. As of June 30, 2015, the Program's current loan balance of ARRA loans was \$11.9 million which was funded with ARRA and other Program funds

Through the years ended June 30, 2015 and 2014, \$629.9 million and \$624.8 million, respectively, in cumulative loans had been approved for funding. At June 30, 2015 and 2014, \$43.9 million and \$62.3 million, respectively, remained encumbered and awaiting disbursement to loan recipients.

### Note 4: Bonds Payable

Bonds payable were as follows at June 30:

<i>(In thousands)</i>				
Series	Interest Rate Range	Final Maturity Dates	2015	2014
2009-A Serial	2.50% – 4.00%	6/1/2018	\$ 5,005	\$ 6,525
2011-A Serial	2.00% – 4.00%	6/1/2015	-	1,730
2011-C Serial	3.25% – 5.00%	6/1/2028	<u>30,290</u>	<u>31,965</u>
			35,295	40,220
	Unamortized premiums		<u>3,242</u>	<u>3,880</u>
			<u>\$ 38,537</u>	<u>\$ 44,100</u>

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

Activity in bonds payable for 2015 was as follows:

<i>(In thousands)</i>	<b>Beginning Balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>Ending Balance</b>	<b>Amount Due within One Year</b>
2009-A	\$ 6,525	\$ -	\$ (1,520)	\$ 5,005	\$ 1,600
2011-A	1,730	-	(1,730)	-	-
2011-C	<u>31,965</u>	<u>-</u>	<u>(1,675)</u>	<u>30,290</u>	<u>2,400</u>
Total bonds payable	<u>\$ 40,220</u>	<u>\$ -</u>	<u>\$ (4,925)</u>	<u>\$ 35,295</u>	<u>\$ 4,000</u>

The principal amount shown above differs from the amount on the statement of net position due to unamortized premiums of approximately \$3.2 million.

Activity in bonds payable for 2014 was as follows:

<i>(In thousands)</i>	<b>Beginning Balance</b>	<b>Additions</b>	<b>Reductions</b>	<b>Ending Balance</b>	<b>Amount Due within One Year</b>
2009-A	\$ 8,005	\$ -	\$ (1,480)	\$ 6,525	\$ 1,520
2011-A	11,360	-	(9,630)	1,730	1,730
2011-C	<u>32,655</u>	<u>-</u>	<u>(690)</u>	<u>31,965</u>	<u>1,675</u>
Total bonds payable	<u>\$ 52,020</u>	<u>\$ -</u>	<u>\$ (11,800)</u>	<u>\$ 40,220</u>	<u>\$ 4,925</u>

The principal amount shown above differs from the amount on the statement of net position due to unamortized premiums of approximately \$3.9 million.

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

Annual debt service requirements to maturity for bonds payable are as follows:

<i>(In thousands)</i>	Principal	Interest
Fiscal year ending June 30,		
2016	\$ 4,000	\$ 1,595
2017	4,075	1,419
2018	4,080	1,249
2019	2,920	1,079
2020	2,745	933
2021 – 2025	12,710	2,694
2026 – 2028	4,765	276
	35,295	9,245
Unamortized premiums	3,242	-
	\$ 38,537	\$ 9,245

In the current fiscal year, the Program did not have any new bond issuances.

In the prior fiscal year, the Program redistributed the bond proceeds from 2011 Revolving Loan Fund Revenue Bonds, Series C (Series 2011 C) between the Program and the State of Arkansas Safe Drinking Water Revolving Loan Fund Program. The distribution resulted in a net decrease in bonds payable of \$5,000. The Series 2011 C was issued by both the Program and State of Arkansas Safe Drinking Water Revolving Loan Fund Program. The redistribution of 2011 C should not have an effect on the bondholders.

### Note 5: Significant Estimates and Concentrations

Accounting principles generally accepted in the United States of America require disclosure of certain significant estimates and current vulnerabilities due to certain concentrations. Those matters include the following:

#### ***Economic Dependency***

Historically, the Program has been economically dependent upon revenue from EPA, but in the current year the Program's federal funds has decreased. The impact of the revenue varies from year to year, and, for the year ended June 30, 2015 and 2014, the Program received 23% and 49%, respectively, of total revenue in the form of federal grants. As of June 30, 2015 and 2014, the Program has \$8.8 million of the Federal Fiscal Year 2014 grant and \$2.0 million of the Federal Fiscal Year 2013 grant remaining to disburse, respectively.

# State of Arkansas Construction Assistance Revolving Loan Fund Program

## Notes to Financial Statements

June 30, 2015 and 2014

### **Principal Forgiveness Loans**

In the fiscal year 2013, the Program began funding principal forgiveness loans (PF) with Base federal capitalization grant funds. EPA required, as part of the Base capitalization grant requirements, that a percentage of the grant be available as subsidy to eligible borrowers. With the federal fiscal year 2010 and 2011 capitalization grant, at least 30% of the grant would be in the form of forgiveness of principal, negative interest loans or grants. The percentage was changed to be not less than 20%, but not greater than 30% of the federal fiscal year 2012 – 2014 grants. However, the above requirement only applies to the portion of the total Base capitalization grant federal appropriation that exceeds \$1 billion. To be eligible to receive subsidy, the borrower must show either:

1. The annual utility rates on 4,000 gallons of water is at least 1.5% of the Medium Household Income for the project area, or
2. At least 51% of the benefiting customers have either Low or Moderate Income as defined by the U. S. Department of Housing and Urban Development Community Development Block Grant Program and the utility rates are at least 1.25% of the Medium Household Income.

The chart below shows the minimum and maximum allowed for principal forgiveness loans:

*(In thousands)*

Federal Fiscal Year	Grant Award Amount	PF Minimum Amount	PF Maximum Amount	Cumulative Disbursements	PF Amount Remaining to Fund
2010	\$ 13,328	\$ 1,996	\$ 6,654	\$ 1,996	\$ -
2011	9,657	895	2,983	362	533
2012	9,239	513	770	-	513
2013	8,722	411	616	-	411
2014	9,165	499	748	-	499
				<u>\$ 2,358</u>	<u>\$ 1,956</u>

The Program has allocated the minimum for each Base Capitalization grant.

The Program forgives the loans as the construction draws are disbursed. In fiscal year 2015 and 2014, \$116,000 and \$1.6 million in principal forgiveness loans were expensed, respectively.

# **State of Arkansas Construction Assistance Revolving Loan Fund Program**

## **Notes to Financial Statements**

**June 30, 2015 and 2014**

### ***Contingencies***

The Program is capitalized by state and federal grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustments by the grantor agencies; therefore, to the extent that the Program has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectability of any related receivable may be impaired. In the opinion of the management of the Program, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants; therefore, no provision has been recorded in the accompanying financial statements for such a contingency.



## **Supplementary Information**

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program  
Combining Statement of Net Position  
June 30, 2015**

(In thousands)

	Revolving Loan Fund	Fees and Expenses	Total
<b>Current Assets</b>			
Cash and cash equivalents	\$ 99,221	\$ 1,941	\$ 101,162
Accrued interest receivable			
Investments	151	3	154
Loans	258	-	258
Accounts receivable			
Borrowers	-	154	154
Investments – current portion	<u>53,715</u>	<u>6,000</u>	<u>59,715</u>
Total current assets	<u>153,345</u>	<u>8,098</u>	<u>161,443</u>
<b>Noncurrent Assets</b>			
Loans receivable – restricted			
Construction	224,951	-	224,951
Wetlands mitigation	<u>153</u>	<u>780</u>	<u>933</u>
Total noncurrent assets	<u>225,104</u>	<u>780</u>	<u>225,884</u>
Total assets	<u>378,449</u>	<u>8,878</u>	<u>387,327</u>
<b>Deferred Outflow of Resources</b>			
Deferred charge on refunding	<u>20</u>	<u>-</u>	<u>20</u>
<b>Current Liabilities</b>			
Accounts payable	-	184	184
Accrued interest payable	133	-	133
Bonds payable – current portion	<u>4,000</u>	<u>-</u>	<u>4,000</u>
Total current liabilities	<u>4,133</u>	<u>184</u>	<u>4,317</u>
<b>Noncurrent Liabilities</b>			
Bonds payable, net of unamortized premiums	<u>34,537</u>	<u>-</u>	<u>34,537</u>
Total liabilities	<u>38,670</u>	<u>184</u>	<u>38,854</u>
<b>Net Position</b>			
Restricted by bond resolution and program requirements	<u>\$ 339,799</u>	<u>\$ 8,694</u>	<u>\$ 348,493</u>

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program**  
Combining Statement of Revenues, Expenses and Changes in Net Position  
Year Ended June 30, 2015

<i>(In thousands)</i>	<b>Revolving Loan Fund</b>	<b>Fees and Expenses</b>	<b>Total</b>
<b>Operating Revenues</b>			
Interest on investments	\$ 477	\$ 6	\$ 483
Interest on loans	5,019	-	5,019
Financing fees	-	2,545	2,545
Net depreciation of investments	<u>(432)</u>	<u>(2)</u>	<u>(434)</u>
Total operating revenues	<u>5,064</u>	<u>2,549</u>	<u>7,613</u>
<b>Operating Expenses</b>			
Program administration	-	239	239
Federal financial assistance			
Base	116	-	116
Bond interest	1,803	-	1,803
Amortization of bond premiums	<u>(638)</u>	<u>-</u>	<u>(638)</u>
Total operating expenses	<u>1,281</u>	<u>239</u>	<u>1,520</u>
<b>Operating Income</b>	<u>3,783</u>	<u>2,310</u>	<u>6,093</u>
<b>Nonoperating Revenue</b>			
Base federal grants	<u>2,001</u>	<u>322</u>	<u>2,323</u>
Total nonoperating revenue	<u>2,001</u>	<u>322</u>	<u>2,323</u>
<b>Income Before Transfers In (Out), Net</b>	5,784	2,632	8,416
<b>Transfers In (Out), Net</b>	<u>2,836</u>	<u>(2,516)</u>	<u>320</u>
<b>Change in Net Position</b>	8,620	116	8,736
<b>Net Position, Beginning of Year</b>	<u>331,179</u>	<u>8,578</u>	<u>339,757</u>
<b>Net Position, End of Year</b>	<u>\$ 339,799</u>	<u>\$ 8,694</u>	<u>\$ 348,493</u>

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program  
Combining Statement of Cash Flows  
Year Ended June 30, 2015**

<i>(In thousands)</i>	<b>Revolving Loan Fund</b>	<b>Fees and Expenses</b>	<b>Total</b>
<b>Operating Activities</b>			
Interest received on investments	\$ 343	\$ 2	\$ 345
Interest received on loans	5,289	-	5,289
Financing fee income received	-	2,647	2,647
Loan disbursements	(23,776)	-	(23,776)
Principal repayments on loans	58,596	-	58,596
Cash paid for interest	(1,804)	-	(1,804)
Federal grant funds expended	(116)	-	(116)
Cash paid for program administration	<u>-</u>	<u>(268)</u>	<u>(268)</u>
Net cash provided by operating activities	<u>38,532</u>	<u>2,381</u>	<u>40,913</u>
<b>Noncapital Financing Activities</b>			
Repayment of long-term debt	(4,925)	-	(4,925)
Transfers in (out)	2,836	(2,516)	320
Nonoperating grants received	<u>2,001</u>	<u>337</u>	<u>2,338</u>
Net cash used in noncapital financing activities	<u>(88)</u>	<u>(2,179)</u>	<u>(2,267)</u>
<b>Investing Activities</b>			
Proceeds from maturities of investments	64,996	2,001	66,997
Purchase of investments	<u>(79,329)</u>	<u>(8,002)</u>	<u>(87,331)</u>
Net cash used in investing activities	<u>(14,333)</u>	<u>(6,001)</u>	<u>(20,334)</u>
<b>Increase (Decrease) in Cash and Cash Equivalents</b>	24,111	(5,799)	18,312
<b>Cash and Cash Equivalents, Beginning of Year</b>	<u>75,110</u>	<u>7,740</u>	<u>82,850</u>
<b>Cash and Cash Equivalents, End of Year</b>	<u>\$ 99,221</u>	<u>\$ 1,941</u>	<u>\$ 101,162</u>

**State of Arkansas Construction Assistance  
Revolving Loan Fund Program  
Combining Statement of Cash Flows (Continued)  
Year Ended June 30, 2015**

<i>(In thousands)</i>	<b>Revolving Loan Fund</b>	<b>Fees and Expenses</b>	<b>Total</b>
<b>Reconciliation of Operating Income to Net Cash (Used In) Provided By Operating Activities</b>			
Operating income	\$ 3,783	\$ 2,310	\$ 6,093
Items not requiring (providing) operating activities cash flows			
Amortization of bond premiums	(638)	-	(638)
Amortization of deferred charge on refunding	16	-	16
Net depreciation of investments	432	2	434
Changes in			
Accrued interest receivable			
Investments	(134)	(4)	(138)
Loans	270	-	270
Accounts receivable – borrowers	-	102	102
Loans receivable	34,820	-	34,820
Accounts payable	-	(29)	(29)
Accrued interest payable	<u>(17)</u>	<u>-</u>	<u>(17)</u>
Net cash provided by operating activities	<u>\$ 38,532</u>	<u>\$ 2,381</u>	<u>\$ 40,913</u>