State of Arkansas Construction Assistance Revolving Loan Fund Program

Accountants' Report and Financial Statements

June 30, 2012 and 2011

BKD LLP
CPAs & Advisors

State of Arkansas Construction Assistance Revolving Loan Fund Program

June 30, 2012 and 2011

Contents

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Independent Accountants' Report on Financial Statements and Supplementary Information

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) as of and for the years ended June 30, 2012 and 2011, as listed in the table of contents. These financial statements are the responsibility of the Program's management. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in *Note 1*, the financial statements of the Program are intended to present the financial position and the results of its operations 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, 2012 and 2011, and the changes in its financial position and its cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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, 2012 and 2011, and its changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis information 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.

Our audit was 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 audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

BKD, LLP

October 30, 2012

State of Arkansas Construction Assistance Revolving Loan Fund Program

Management's Discussion and Analysis

June 30, 2012 and 2011

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, 2012, basic financial statements include three required statements: The statement of net assets; the statement of revenues, expenses and changes in net assets; and the statement of cash flows. Comparative totals as of and for the years ended June 30, 2011 and 2010, 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 assets; the combining statement of revenues, expenses and changes in net assets; 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 Assets

(In thousands)

	2012	2011	2010
Total assets	$ 377,679	$ 332,143	$ 334,619
Current liabilities	11,724	11,794	8,041
Noncurrent liabilities	56,752	29,228	51,360
Total liabilities	68,476	41,022	59,401
Total net assets – restricted for program requirements	$ 309,203	$ 291,121	$ 275,218

At June 30, 2012, the Program's total assets of $377.7 million increased $45.5 million from June 30, 2011. The Program's total assets of $332.1 million at June 30, 2011, reflected a decrease of $2.5 million from June 30, 2010. In the current year, the Program had increases in cash and cash equivalents and investments of $65.7 million, which were offset by a decline of $20.3 million in loans receivable. The Program received $18.0 million in loan prepayments from borrowers. For the prior year, the Program had decreases in investments of $16.6 million and in loans receivable of $3.8 million, which were offset by increases in cash and cash equivalents of $17.6 million.

The following table reports loan activity for each year (in thousands):

	2012	2011	2010
Loan disbursements	$ 19,017	$ 17,996	$ 35,471
Loan repayments	39,280	21,759	21,412
Net (decrease) increase in loans receivable	$ (20,263)	$ (3,763)	$ 14,059

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

	2012	2011	2010
New loans	$ 90,000	$ 4,150	$ 11,256
Loan disbursements – new loans	10,050	2,376	3,846
Existing loans	79,691	79,596	77,855
Loan disbursements – existing loans	8,187	15,620	31,625

The Program continually made loans from federal grant funds from the U.S. Environmental Protection Agency (EPA) state matching funds and revolving Program funds. The Program received federal funds in the form of an annual capitalization grant (Base) and a 2010 American Recovery and Reinvestment Act (ARRA) grant. In the current year, as encouraged by EPA, the Program focused on utilizing federal funds, when available, to fund loans. The Program continued to use 2009 Issue Prepayment funds and revolving program funds. The table below reflects the amounts used from each funding source for fiscal years 2012, 2011 and 2010 (in thousands):

	2012	2011	2010
EPA Federal			
Base	$ 11,999	$ 2,627	$ 4,220
ARRA	2,392	6,585	3,746
State Matching	1,588	2,201	879
2009 Issue Prepayment Funds	1,008	936	1,940
Revolving Program Funds	1,250	5,647	24,686
Administrative Funds	780	-	-
	$ 19,017	$ 17,996	$ 35,471

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

The federal fiscal year 2012 Base grant has been approved by the Environmental Protection Agency in the amount of $9.2 million and will be available in October 2012.

The Program's total liabilities increased to $68.5 million at June 30, 2012, from $41.0 million at June 30, 2011, and from $59.4 million at June 30, 2010. The increase was attributed to the issuance of the $57.0 million Revolving Loan Fund Revenue Bonds, Series 2011 C (Series 2011 C). These bonds were issued by the Program and the Safe Drinking Water Revolving Loan Fund Program. The Program's portion of the Series 2011 C issue was $32.7 million plus $5.1 million for bond premiums, which was offset by scheduled redemptions paid of $11.3 million. For the fiscal year ended June 30, 2011, the Program refunded $41.0 million 2001 Series A bonds and 2004 Series A bonds with $11.8 million 2011 Refunding Series A and $19.4 million in 2011 Refunding Taxable Series B bonds along with other available funds, which resulted in a decline of $9.8 million in the bonds outstanding. The Program had scheduled bond redemptions of $6.2 million for fiscal year ended June 30, 2011.

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

(In thousands)

	2012	2011	2010
Total interest income	$ 5,500	$ 5,858	$ 6,386
Other income	2,475	2,502	2,693
Total operating revenues	7,975	8,360	9,079
Total interest on bonds and notes	4,080	2,975	2,891
Total amortization expense	(600)	(264)	44
Federal financial assistance	91	3,836	8,985
Administrative expense	252	267	288
Total operating expenses	3,823	6,814	12,208
Operating income (loss)	4,152	1,546	(3,129)
Transfers (out) in, net	(1,080)	919	(1,080)
Base federal grants	12,528	3,017	4,397
ARRA federal grants	2,482	10,421	12,731
Change in net assets	18,082	15,903	12,919
Net assets			
Beginning of year	291,121	275,218	262,299
End of year	$ 309,203	$ 291,121	$ 275,218

Total operating revenue has continuously decreased over the past three years. Operating revenue declined $385,000 and $719,000 during fiscal years 2012 and 2011, respectively. During the current year, the Program's loan mortgage interest income declined $279,000 and investment interest income declined $79,000. The decline in mortgage interest income was attributable to the decline in loan balances mainly due to receiving approximately $18.0 million in prepayments during the year. The decline in investment interest income was attributable to investments not being purchased until the last quarter of the fiscal year and funds remaining in cash with extremely low rates. In the prior year, investment income and net depreciation of investments declined $568,000 due to the Program liquidating debt service reserve accounts, which consisted of guaranteed investment contracts and U.S. agencies obligations with an average interest rate of 4.0%. These liquidated funds were used to extinguish debt of the Program.

Base federal grants revenue increased $9.5 million in the current fiscal year. The ARRA federal grants declined $7.9 million in the current year. As of June 30, 2012, the Program had expended $14.6 million of a $19.7 million Base federal grants awarded. Information regarding when Base federal grant awards were expended for construction draws is as follows (in thousands):

Federal Award Year	Beginning Balance	Amount Expended in FY2010	Amount Expended in FY2011	Amount Expended in FY2012
2009	$ 4,220	$ 4,220	$ -	$ -
2010	12,795	-	2,627	7,557
2011	6,953	-	-	4,442
		$ 4,220	$ 2,627	$ 11,999

The Program received ARRA federal funding of $2.5 million. The funds were expended in the form of principal forgiveness and repayable loans as follows (in thousands):

Type of Loans	Amount
Principal forgiveness loans	$ 91
Repayable loans	$ 2,391

The Program continues to fund loans from other revenue sources including $3.8 million from the Program funds, state match funds and loan prepayments.

Revenues from investments were $136,000, $215,000 and $537,000 for fiscal years ended June 30, 2012, 2011 and 2010, respectively. The average return on cash, cash equivalents and investments was 0.03%, 0.36% and 0.42% for years ended June 30, 2012, 2011 and 2010, respectively. The Program maintains liquidity to fund projects as needed. Higher cash and cash equivalent balances were maintained during the current and prior years as the Program evaluated liquidity needs and investment options in the current economic climate.

Operating expenses decreased by $3.0 million and $5.4 million during 2012 and 2011, respectively. In fiscal year 2012, the Program expensed $91,000 in principal forgiveness loans funded by the ARRA federal grant funds as compared to $3.8 million in fiscal year 2011. The Program's interest on bonds and notes increased $1.1 million in fiscal year 2012, which was attributable to the interest on the Series 2011 C issue. Program administration expenses totaled $252,000, $267,000 and $288,000 for the fiscal years ended June 30, 2012, 2011 and 2010, 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 fiscal year 2012, the Program funded state match from funds within the Program and transferred out $1.1 million to Arkansas National Resources Commission (ANRC) for administrating the Program. The funding source for the administrative fee is 4% of the EPA capitalization grant along with funds from the Fees and Expenses Fund.

In fiscal year 2011, the Program received $2.0 million from the ANRC Water, Waste Disposal and Pollution Abatement Facilities General Obligation Bond Fund Program for state match. The Program transferred out $1.1 million to ANRC for administrating the Program.

The net assets of the Program increased $34.0 million in the past two years. The bond resolutions and the Program restrict all of the net assets.

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 Assets

June 30, 2012 and 2011

(In thousands)	2012	2011
Current Assets		
Cash and cash equivalents	$ 122,201	$ 77,095
Accrued interest receivable		
Investments	41	16
Loans	375	370
Accounts receivable		
Borrowers	124	177
Environmental Protection Agency	386	390
Investments – current portion	29,310	8,606
Total current assets	152,437	86,654
Noncurrent Assets		
Investments – restricted	2,676	2,752
Loans receivable – restricted		
Construction	221,128	242,169
Wetlands mitigation	933	155
Other assets	505	413
Total noncurrent assets	225,242	245,489
Total assets	377,679	332,143
Current Liabilities		
Accounts payable	202	391
Accrued interest payable	202	93
Bonds payable – current portion	11,320	11,310
Total current liabilities	11,724	11,794
Noncurrent Liabilities		
Deferred fees	371	587
Bonds payable, net of unamortized premiums (discounts)	56,381	28,641
Total noncurrent liabilities	56,752	29,228
Total liabilities	68,476	41,022
Net Assets		
Restricted for program requirements	$ 309,203	$ 291,121

State of Arkansas Construction Assistance Revolving Loan Fund Program

Statements of Revenues, Expenses and Changes in Net Assets

Years Ended June 30, 2012 and 2011

(In thousands)	2012	2011
Operating Revenues		
Interest on investments	$ 136	$ 215
Interest on loans	5,364	5,643
Financing fees	2,542	2,581
Net depreciation of investments	(75)	(85)
Other	8	6
Total operating revenues	7,975	8,360
Operating Expenses		
Program administration	252	267
Federal financial assistance	91	3,836
Bond interest	4,080	2,975
Amortization of bond issuance costs	154	104
Amortization of bond discounts and premiums	(754)	(368)
Total operating expenses	3,823	6,814
Operating Income	4,152	1,546
Nonoperating Revenue		
Base federal grants	12,528	3,017
American Recovery and Reinvestment Act federal grants	2,482	10,421
Total nonoperating revenue	15,010	13,438
Income Before Transfers (Out) In, Net	19,162	14,984
Transfers (Out) In, Net	(1,080)	919
Change in Net Assets	18,082	15,903
Net Assets, Beginning of Year	291,121	275,218
Net Assets, End of Year	$ 309,203	$ 291,121

State of Arkansas Construction Assistance Revolving Loan Fund Program

Statements of Cash Flows

Years Ended June 30, 2012 and 2011

(In thousands)	2012	2011
Operating Activities		
Interest received on investments	$ 110	$ 380
Interest received on loans	5,359	5,662
Financing fee income received	2,380	2,385
Loan disbursements	(19,017)	(17,996)
Principal repayments on loans	39,280	21,759
Cash paid for interest	(1,880)	(2,624)
Federal grant funds expended	(91)	(3,836)
Cash paid for program administration	(434)	(245)
Net cash provided by operating activities	25,707	5,485
Noncapital Financing Activities		
Repayment of long-term debt	(11,310)	(50,284)
Proceeds from bond issuance	37,722	32,219
Cash paid for cost of issuance of long-term debt	(246)	(300)
Transfers (out) in	(1,080)	919
Nonoperating grants received	15,015	13,048
Net cash provided by (used in) noncapital financing activities	40,101	(4,398)
Investing Activities		
Proceeds from maturities of investments	8,729	53,889
Purchase of investments	(29,431)	(37,416)
Net cash (used in) provided by investing activities	(20,702)	16,473
Increase in Cash and Cash Equivalents	45,106	17,560
Cash and Cash Equivalents, Beginning of Year	77,095	59,535
Cash and Cash Equivalents, End of Year	$ 122,201	$ 77,095

State of Arkansas Construction Assistance Revolving Loan Fund Program

Statements of Cash Flows (Continued)

Years Ended June 30, 2012 and 2011

(In thousands)	2012	2011
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating income	$ 4,152	$ 1,546
Items not requiring (providing) operating activities cash flows		
Amortization of bond issuance costs	154	104
Amortization of bond discounts and premiums	1,336	115
Amortization of deferred financing fees	(216)	(205)
Net depreciation of investments	75	85
Changes in		
Accrued interest receivable		
Investments	(25)	54
Loans	(5)	18
Accounts receivable – borrowers	53	9
Loans receivable	20,263	3,763
Accounts payable	(189)	120
Accrued interest payable	109	(132)
Other assets	-	8
Net cash provided by operating activities	$ 25,707	$ 5,485

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, 2012 and 2011, were $185,000 and $201,000, 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, 2012 and 2011, the AAWQLP had $18.9 million and $21.4 million, respectively, in deposits and investments with various financial institutions.

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 assets. 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.

Pursuant to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, the Program has elected not to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB) issued after November 30, 1989.

Recently Issued Accounting Pronouncements

GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, is effective for periods beginning after December 15, 2011. It provides a new statement of net position format to report all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position (which is the net residual amount of the other elements). This Statement requires that deferred outflows of resources and deferred inflows of resources be reported separately from assets and liabilities. GASB 63 also amends certain provisions of GASB Statement No. 34, Basic Financial Statements — and Management's Discussion and Analysis — for State and Local Governments, and related pronouncements to reflect the residual measure in the statement of financial position as net position, rather than net assets.

In March 2012, the Governmental Accounting Standards Board issued GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. Although the Authority is still determining the impact of this pronouncement, it is expected to affect how the refunding of debt and debt issuance cost are recorded. It is effective for periods beginning after December 15, 2012.

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, 2012 and 2011, cash equivalents of $122.2 million and $77.1 million, respectively, consisted primarily of money market mutual funds with variable interest rates.

Included in cash equivalents on the Program’s statement of net assets is the Fees and Expenses Fund with a balance of approximately $4.1 million and $7.3 million at June 30, 2012 and 2011, respectively. This fund contains fees charged on loans of the Program, as allowed by the U.S. 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 Costs and Discounts and Premiums

Costs related to issuing bonds and discounts and 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 bond issuance costs and discounts and premiums.

Financing Fees

The Program receives monthly financing fees from borrowers. Prior to 2000, the Program charged closing fees that were deferred and are currently being amortized into income ratably over the terms of the bonds outstanding.

Net Assets Restricted by Bond Resolution and Program Requirements

Net assets restricted by bond resolution and program requirements represent 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 the amount of the deposits.

At June 30, 2012 and 2011, respectively, $5.7 million and $6.0 million of the Program's deposits (and carrying value) of $11.6 million and $12.8 million were exposed to custodial credit risk as follows:

(In thousands)	2012	2011
Uninsured and collateral held by pledging financial institution trust department or agent in the Program's name	$ 5,670	$ 6,015

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, 2012 and 2011, the Program had the following investments and maturities:

(In thousands)

		June 30, 2012			
		Maturities in Years			
Type	Fair Value	Less than 1	1–5	6–10	More than 10
U.S. Treasury obligations	$ 12,688	$ 10,012	$ 2,676	$ -	$ -
U.S. agencies obligations	19,298	19,298	-	-	-
Money market mutual funds	110,629	110,629	-	-	-
	$ 142,615	$ 139,939	$ 2,676	$ 0	$ 0

(In thousands)

		June 30, 2011			
		Maturities in Years			
Type	Fair Value	Less than 1	1–5	6–10	More than 10
U.S. Treasury obligations	$ 2,752	$ -	$ 2,752	$ -	$ -
U.S. agencies obligations	8,606	8,606	-	-	-
Money market mutual funds	64,266	64,266	-	-	-
	$ 75,624	$ 72,872	$ 2,752	$ 0	$ 0

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 "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 and guaranteed investment contracts 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 Farm Credit Bank	$	7,298	5%
Federal Home Loan Bank		7,001	5%

Summary of Carrying Values

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

(In thousands)		2012		2011
Carrying value				
Deposits	$	11,572	$	12,829
Investments		142,615		75,624
	$	154,187	$	88,453
Included in the following statement of net assets captions				
Cash and cash equivalents	$	122,201	$	77,095
Investments – current portion		29,310		8,606
Investments – restricted		2,676		2,752
	$	154,187	$	88,453

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, 2012 and 2011, such loans had a carrying value of approximately $222.1 million and $242.3 million, respectively, of which approximately $65.0 million and $67.3 million, respectively, are for projects still under construction. The loans bear interest ranging from 0.0% to 4.0%, and are collateralized by special assessments, by user charges or by 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, 2012 and 2011, the Program had cumulatively funded $12.7 million and $10.3 million, respectively, in ARRA loans.

Through the years ended June 30, 2012 and 2011, $544.5 million and $454.5 million, respectively, in cumulative loans had been approved for funding. At June 30, 2012 and 2011, $84.6 million and $12.8 million, respectively, remained encumbered and awaiting disbursement to loan recipients.

Note 4: Bonds Payable

Bonds payable were as follows at June 30:

(In thousands)

Series	Interest Rate Range	Final Maturity Dates	2012	2011
2009-A				
Serial	2.50% – 4.00%	6/1/2018	$ 9,420	10,770
2011-A				
Serial	2.00% – 4.00%	6/1/2015	11,825	11,825
2011-B				
Serial Taxable	.75% – 1.20%	6/1/2013	9,440	19,400
2011-C				
Serial	3.25% – 5.00%	6/1/2028	32,655	-
			63,340	41,995
	Unamortized premiums and discounts		4,361	(2,044)
			$ 67,701	$ 39,951

Activity in bonds payable for 2012 was as follows:

(In thousands)	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due within One Year
2009-A	$ 10,770	$ -	$ (1,350)	$ 9,420	$ 1,415
2011-A	11,825	-	-	11,825	465
2011-B	19,400	-	(9,960)	9,440	9,440
2011-C	-	32,655	-	32,655	-
Total bonds payable	$ 41,995	$ 32,655	$ (11,310)	$ 63,340	$ 11,320

The principal amount shown above differs from the amount on the statement of net assets due to unamortized premiums and discounts of approximately $4.4 million.

Activity in bonds payable for 2011 was as follows:

(In thousands)	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due within One Year
2001-A	$ 25,800	$ -	$ (25,800)	$ -	$ -
2004-A	20,050	-	(20,050)	-	-
2009-A	12,060	-	(1,290)	10,770	1,350
2011-A	-	11,825	-	11,825	-
2011-B	-	19,400	-	19,400	9,960
Total bonds payable	$ 57,910	$ 31,225	$ (47,140)	$ 41,995	$ 11,310

The principal amount shown above differs from the amount on the statement of net assets due to unamortized discounts and premiums of approximately $2.0 million.

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

(In thousands)	Principal	Interest
Fiscal year ending June 30,		
2013	$ 11,320	$ 2,418
2014	11,110	2,246
2015	4,805	1,824
2016	4,335	1,620
2017	4,320	1,428
2018 – 2022	15,430	4,597
2023 – 2027	10,270	1,544
2028 – 2032	1,750	62
	63,340	15,739
Unamortized discounts and premiums	4,361	-
	$ 67,701	$ 15,739

In the current fiscal year, ADFA issued $57.0 million in 2011 Revolving Loan Fund Revenue Bonds, Series C (Series 2011 C). The Series 2011 C bond issue was a combined issue between the Program and the State of Arkansas Safe Drinking Water Revolving Loan Fund Program. This issue offered the two programs the option of the cross collateralization transfers which provides strength and stability in making the debt service payments. The Series 2011 C was rated "AAA" by Standard & Poor's and Fitch Ratings. The portion of the Series 2011 C bond issue allocated to the Program was $32.7 million.

During the prior fiscal year, ADFA issued $31.2 million in 2011 Refunding Series A and 2011 Refunding Taxable Series B bonds for the benefit of the Program. The proceeds from the sale of the Series Refunding A bonds, along with other funds, were used to current refund all the outstanding 2004 Series A bonds on June 1, 2011, and to pay underwriters compensation and other costs of issuance. With the issuance of the 2011 Refunding Taxable Series B bonds, the Program defeased all the outstanding 2001 Series A bonds. The proceeds from the bonds, along with other funding sources, were deposited in trust under an escrow agreement sufficient in amount to pay principal and interest on the defeased bonds on May 26, 2011, and were used to pay underwriters compensation and other costs of issuance. The advance refunding resulted in an extinguishment of debt since the Program was legally released from its obligation on the 2001 Series A bonds at the time of defeasance.

The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of $3.5 million. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2015 using the effective-interest method. The Program completed the refunding to reduce its total debt service payments over the next seven years by $9.8 million and to obtain a present value benefit (difference between the present values of the old and new debt service payments) of $1.6 million for the Program.

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

The Program has been economically dependent upon revenue from EPA. The impact of the revenue varies from year to year, and, for the year ended June 30, 2012 and 2011, the Program received 65% and 62%, respectively, of total revenue in the form of federal grants. In the current year, the Program has disbursed $2.5 million of the ARRA grant funds and $12.5 million of Base grant funds. In the prior fiscal year, the Program has disbursed $10.4 million of the ARRA grant funds and $3.0 million of Base grant funds. As of June 30, 2012, $2.6 million of the $12.8 million fiscal year 2010 Base grant and $2.5 million of the $7.0 million fiscal year 2011 Base grant is still to be disbursed.

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.

In conjunction with the issuance of tax-exempt bonds, the Internal Revenue Code of 1986 establishes rules and regulations for arbitrage rebates. The Program has made provisions for revenues above the rebate limit, which must be remitted to the federal government.

Supplementary Information

State of Arkansas Construction Assistance Revolving Loan Fund Program

Combining Statement of Net Assets

June 30, 2012

(In thousands)	Revolving Loan Fund	Fees and Expenses	Total
Current Assets			
Cash and cash equivalents	$ 118,119	$ 4,082	$ 122,201
Accrued interest receivable			
Investments	22	19	41
Loans	375	-	375
Accounts receivable			
Borrowers	-	124	124
Environmental Protection Agency	-	386	386
Investments – current portion	27,311	1,999	29,310
Total current assets	145,827	6,610	152,437
Noncurrent Assets			
Investments – restricted	-	2,676	2,676
Loans receivable – restricted			
Construction	221,128	-	221,128
Wetlands mitigation	153	780	933
Other assets	505	-	505
Total noncurrent assets	221,786	3,456	225,242
Total assets	367,613	10,066	377,679
Current Liabilities			
Accounts payable	14	188	202
Accrued interest payable	202	-	202
Bonds payable – current portion	11,320	-	11,320
Total current liabilities	11,536	188	11,724
Noncurrent Liabilities			
Deferred fees	3	368	371
Bonds payable, net of unamortized premiums (discounts)	56,381	-	56,381
Total noncurrent liabilities	56,384	368	56,752
Total liabilities	67,920	556	68,476
Net Assets			
Restricted for program requirements	$ 299,693	$ 9,510	$ 309,203

State of Arkansas Construction Assistance Revolving Loan Fund Program

Combining Statement of Revenues, Expenses and Changes in Net Assets

Year Ended June 30, 2012

(In thousands)	Revolving Loan Fund	Fees and Expenses	Total
Operating Revenues			
Interest on investments	$ 13	$ 123	$ 136
Interest on loans	5,364	-	5,364
Financing fees	11	2,531	2,542
Net appreciation (depreciation) of investments	1	(76)	(75)
Other	8	-	8
Total operating revenues	5,397	2,578	7,975
Operating Expenses			
Program administration	-	252	252
Federal financial assistance	91	-	91
Bond interest	4,080	-	4,080
Amortization of bond issuance costs	154	-	154
Amortization of bond discounts and premiums	(754)	-	(754)
Total operating expenses	3,571	252	3,823
Operating Income	1,826	2,326	4,152
Nonoperating Revenue			
Base federal grants	11,999	529	12,528
American Recovery and Reinvestment Act federal grants	2,482	-	2,482
Total nonoperating revenue	14,481	529	15,010
Income Before Transfers In (Out)	16,307	2,855	19,162
Transfers In (Out)	2,077	(3,157)	(1,080)
Change in Net Assets	18,384	(302)	18,082
Net Assets, Beginning of Year	281,309	9,812	291,121
Net Assets, End of Year	$ 299,693	$ 9,510	$ 309,203

State of Arkansas Construction Assistance Revolving Loan Fund Program

Combining Statement of Cash Flows

Year Ended June 30, 2012

(In thousands)	Revolving Loan Fund	Fees and Expenses	Total
Operating Activities			
Interest (paid) received on investments	$ (8)	$ 118	$ 110
Interest received on loans	5,359	-	5,359
Financing fee income received	-	2,380	2,380
Loan disbursements	(18,238)	(779)	(19,017)
Principal repayments on loans	39,280	-	39,280
Cash paid for interest	(1,880)	-	(1,880)
Federal grant funds expended	(91)	-	(91)
Cash paid for program administration	(168)	(266)	(434)
Net cash provided by operating activities	24,254	1,453	25,707
Noncapital Financing Activities			
Repayment of long-term debt	(11,310)	-	(11,310)
Proceeds from bond issuance	37,722	-	37,722
Cash paid for cost of issuance of long-term debt	(246)	-	(246)
Transfers in (out)	2,077	(3,157)	(1,080)
Nonoperating grants received	14,482	533	15,015
Net cash provided by (used in) noncapital financing activities	42,725	(2,624)	40,101
Investing Activities			
Proceeds from maturities of investments	8,729	-	8,729
Purchase of investments	(27,431)	(2,000)	(29,431)
Net cash used in investing activities	(18,702)	(2,000)	(20,702)
Increase in Cash and Cash Equivalents	48,277	(3,171)	45,106
Cash and Cash Equivalents, Beginning of Year	69,842	7,253	77,095
Cash and Cash Equivalents, End of Year	$ 118,119	$ 4,082	$ 122,201

State of Arkansas Construction Assistance Revolving Loan Fund Program

Combining Statement of Cash Flows (Continued)

Year Ended June 30, 2012

(In thousands)	Revolving Loan Fund	Fees and Expenses	Total
Reconciliation of Operating Income to Net Cash Provided By Operating Activities			
Operating income	$ 1,826	$ 2,326	$ 4,152
Items not requiring (providing) operating activities cash flows			
Amortization of bond issuance costs	154	-	154
Amortization of bond discounts and premiums	1,336	-	1,336
Amortization of deferred financing fees	(10)	(206)	(216)
Net (appreciation) depreciation of investments	(1)	76	75
Changes in			
Accrued interest receivable			
Investments	(20)	(5)	(25)
Loans	(5)	-	(5)
Accounts receivable – borrowers	-	53	53
Loans receivable	21,042	(779)	20,263
Accounts payable	(177)	(12)	(189)
Accrued interest payable	109	-	109
Net cash provided by operating activities	$ 24,254	$ 1,453	$ 25,707