

**State of Arkansas Safe Drinking Water
Revolving Loan Fund Program**

Auditor's Report and Financial Statements

June 30, 2013 and 2012



**State of Arkansas Safe Drinking Water
Revolving Loan Fund Program
June 30, 2013 and 2012**

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Independent Auditor's 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, which are comprised of a statement of net position as of June 30, 2013 and 2012, and statements of revenues, expenses and changes in net position and of cash flows for the years then ended and the related notes to the financial statements, as listed in the table of contents, of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program (the Program).

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. 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.

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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, 2013 and 2012, and its changes in financial position and 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 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, 2013 and 2012, 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.

Required Supplementary Information

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.

Supplementary Information

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.

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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

Little Rock, Arkansas
October 31, 2013

**State of Arkansas Safe Drinking Water
Revolving Loan Fund Program
Management's Discussion and Analysis
June 30, 2013 and 2012**

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 Safe Drinking Water 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, 2013, 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, 2012 and 2011, 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, the Fees and Expense Set Aside, the Small System Technical Assistance Set Aside, the Well Head Protection Set Aside, the Capacity Development Set Aside and the State Program Management Set Aside, which comprise the Program.

Condensed Financial Information – Statements of Net Position

(In thousands)

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Total assets	\$ <u>220,022</u>	\$ <u>204,197</u>	\$ <u>162,274</u>
Current liabilities	1,562	600	392
Noncurrent liabilities	<u>29,117</u>	<u>30,717</u>	<u>2,775</u>
Total liabilities	<u>30,679</u>	<u>31,317</u>	<u>3,167</u>
Net position – restricted for program requirements	\$ <u>189,343</u>	\$ <u>172,880</u>	\$ <u>159,107</u>

The Program's total assets have continually increased over the past three years, primarily attributed to growth in the Program's loans for water system projects. Loans receivable – restricted increased to \$160.3 million at June 30, 2013, from \$151.6 million and \$135.6 million at June 30, 2012 and 2011, respectively.

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

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Loan disbursements	\$ 13,216	\$ 19,954	\$ 27,128
Loan repayments	<u>4,514</u>	<u>3,948</u>	<u>3,545</u>
Net increase in loans receivable	<u>\$ 8,702</u>	<u>\$ 16,006</u>	<u>\$ 23,583</u>

Grants from the United States Environmental Protection Agency (EPA) comprised 62%, 39% and 57% of the funding source of the loan disbursements for fiscal years ended June 30, 2013, 2012, and 2011, respectively. The Program received federal funds in the form of a Base annual grant and, in fiscal year 2010, an American Recovery and Reinvestment Act (ARRA) grant. The table below reflects the amounts used from each funding source for fiscal years 2013, 2012 and 2011 as follows (in thousands):

	<u>2013</u>	<u>2012</u>	<u>2011</u>
EPA Federal			
Base	\$ 8,197	\$ 7,855	\$ 10,945
ARRA	-	-	4,605
State Matching	5,019	4,125	3,683
Fees and Expenses Fund	-	-	3,296
Revolving Program Funds	<u>-</u>	<u>7,974</u>	<u>4,599</u>
	<u>\$ 13,216</u>	<u>\$ 19,954</u>	<u>\$ 27,128</u>

The construction period for the loans of the Program is approximately two years.

In fiscal year 2012, the Program began funding principal forgiveness loans from the Base capitalization grant as required by EPA. Each construction draw is forgiven at the time of the draw. For the fiscal years ended 2013 and 2012, the Program has awarded grants to multiple borrowers and has forgiven \$5.4 million and \$178,000, respectively.

The Program maintains liquidity for funding loans. The Program invested excess funds in U.S. Treasury and agencies obligations and in money market mutual funds from time to time to allow for re-evaluation of the Program's liquidity needs. Currently, the Program has \$10 million in investments which will mature in the next fiscal year.

At June 30, 2013, the Program's current liabilities increased \$962,000 from June 30, 2012, and \$208,000 from June 30, 2011 to June 30, 2012. The increases were attributed to the \$1 million current portion of the Revolving Loan Fund Program Revenue Bonds, Series 2011 C (Series 2011 C) bonds payable due in fiscal year 2014 and the payable to the Arkansas Development Finance Authority (ADFA), which was offset by a decline in the payable to the Department of Health (DOH). The amounts due to DOH which reimburses the agency for expenses related to administrating the Program were \$336,000, \$375,000 and \$280,000 at June 30, 2013, 2012 and 2011, respectively, which is reimbursed directly from the EPA Federal Base grant.

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ADFA receives an annual administrative fee, based on a percentage of the fiscal year end outstanding loan balance. The amounts due to ADFA were \$129,000, \$127,000 and \$113,000 for years ended June 30, 2013, 2012 and 2011, respectively.

Noncurrent liabilities reflected a decrease of \$1.6 million. The decrease is attributable to the decline in bonds payable for the amortization of the Series 2011 C premiums and the reclassification of the amount of bonds due in the fiscal year 2014. Deferred fees declined \$165,000, which reflected the amortization of a 3% loan-closing fee, which the Arkansas Natural Resources Commission (ANRC) discontinued in March 2009. In fiscal year 2012, ADFA issued the Series 2011 C bonds in the amount of \$57.0 million for the benefit of the Program and the Construction Assistance Revolving Loan Fund Program of which \$28.1 million is payable by the Program.

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

(In thousands)

	2013	2012	2011
Total interest income	\$ 3,242	\$ 2,978	\$ 2,638
Other income	<u>1,733</u>	<u>1,611</u>	<u>1,426</u>
Total operating revenues	<u>4,975</u>	<u>4,589</u>	<u>4,064</u>
Program administration	167	160	146
Federal financial assistance	5,428	303	5,882
Total interest on bonds	1,175	757	-
Total amortization expense	<u>(414)</u>	<u>(266)</u>	<u>-</u>
Total operating expenses	<u>6,356</u>	<u>954</u>	<u>6,028</u>
Operating (loss) income	(1,381)	3,635	(1,964)
Federal Grants	18,907	11,188	24,585
Transfers (out) in, net	<u>(1,063)</u>	<u>(1,050)</u>	<u>343</u>
Change in net position	16,463	13,773	22,964
Net position			
Beginning of year	<u>172,880</u>	<u>159,107</u>	<u>136,143</u>
End of year	<u>\$ 189,343</u>	<u>\$ 172,880</u>	<u>\$ 159,107</u>

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Included in total interest income is interest earned on loans, which has increased to \$3.2 million for the year ended June 30, 2013, from \$3.0 million for the year ended June 30, 2012, and \$2.6 million for the year ended June 30, 2011. The attributing factor to the increase is the continuous funding of loans at a faster pace than repayments in the Program. Revenues from investments increased to \$39,000 in the current year, attributable to the investment of excess funds in U. S. Treasury and agencies obligations. The average returns on cash, cash equivalents and investments for fiscal year 2013 have increased to 0.06%; whereas the average returns for 2012 and 2011 were 0.02% and 0.05%, respectively.

For fiscal year 2013, operating expenses increased \$5.4 million. The increase was attributed to a \$5.1 million increase related to the forgiveness of principal loans provided by the Base federal funds to various municipalities for water improvements and a net increase of \$270,000 in bond interest expense and amortization of bond issuance costs and premiums on the Series 2011 C bonds.

In comparison for fiscal year 2012, operating expenses declined \$5.1 million. The decrease was due to a decline of \$5.8 million related to the granting of ARRA federal funds to various municipalities for water improvements, which was offset by a net increase of \$491,000 in bond interest expense and amortization of bond issuance cost and premiums on the Series 2011 C bonds. All ARRA funds were disbursed as of June 30, 2012.

For the year ended June 30, 2013, the change in net position of \$16.5 million increased \$2.7 million. The increase was primarily related to the increase in federal grants received of \$7.7 million, which was offset by the increase in federal financial assistance expense of \$5.1 million.

The change in net position of \$13.8 million for the year ended June 30, 2012, declined \$9.2 million in comparison to the fiscal year ended June 30, 2011. The decrease in the change in net position was primarily attributable to the decline of \$13.4 million in federal grants received and the net decrease in transfers in and out of \$1.4 million.

The Program primarily used federal grants for funding loans and paying expenses. These funds were drawn down from the federal government as expenses were incurred by the municipalities, ANRC or DOH.

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The Program received transfers in from the ANRC Water, Waste Disposal and Pollution Abatement Facilities General Obligation Bond Fund Program, which represented the state matching funds for the Program. Transfers in were offset by transfers out to other agencies for the reimbursement of expenses relating to the administration of the Program. The transfers in and out are represented in the following table (in thousands):

	2013	2012	2011
ANRC-state match	\$ 3,305	\$ 2,512	\$ 3,572
Department of Health	(3,688)	(3,042)	(2,709)
ANRC-administration	(680)	(520)	(520)
Transfers (out) in, net	\$ (1,063)	\$ (1,050)	\$ 343

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

Contact Regarding the Program

This financial report is designed to provide 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 Safe Drinking Water Revolving Loan Fund Program

Statements of Net Position

June 30, 2013 and 2012

(In thousands)

	2013	2012
Current Assets		
Cash and cash equivalents	\$ 48,641	\$ 33,616
Accrued interest receivable	280	240
Accounts receivable		
Borrowers	151	147
Environmental Protection Agency	453	375
Investments – current portion	10,001	10,000
Total current assets	59,526	44,378
Noncurrent Assets		
Investments – restricted	-	8,004
Loans receivable – restricted		
Construction	156,273	147,514
Northeast Arkansas Public Water Authority	4,063	4,120
Other assets	160	181
Total noncurrent assets	160,496	159,819
Total assets	220,022	204,197
Current Liabilities		
Accounts payable	464	502
Accrued interest payable	98	98
Bonds payable – current portion	1,000	-
Total current liabilities	1,562	600
Noncurrent Liabilities		
Bonds payable, net of unamortized premiums	26,677	28,112
Deferred fees	2,440	2,605
Total noncurrent liabilities	29,117	30,717
Total liabilities	30,679	31,317
Net Position		
Restricted for program requirements	\$ 189,343	\$ 172,880

**State of Arkansas Safe Drinking Water
Revolving Loan Fund Program**
Statements of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2013 and 2012

(In thousands)

	<u>2013</u>	<u>2012</u>
Operating Revenues		
Interest on investments	\$ 39	\$ 7
Interest on loans	3,203	2,971
Financing fees	1,736	1,613
Net depreciation of investments	<u>(3)</u>	<u>(2)</u>
Total operating revenues	<u>4,975</u>	<u>4,589</u>
Operating Expenses		
Program administration	167	160
Federal financial assistance		
Base federal grants	5,428	178
American Recovery and Reinvestment Act federal grants	-	125
Bond interest	1,175	757
Amortization of bond issuance costs	21	14
Amortization of bond premiums	<u>(435)</u>	<u>(280)</u>
Total operating expenses	<u>6,356</u>	<u>954</u>
Operating (Loss) Income	(1,381)	3,635
Nonoperating Revenue		
Base federal grants	18,907	11,063
American Recovery and Reinvestment Act federal grants	<u>-</u>	<u>125</u>
Total nonoperating revenue	<u>18,907</u>	<u>11,188</u>
Income Before Transfers Out, Net	17,526	14,823
Transfers Out, Net	<u>(1,063)</u>	<u>(1,050)</u>
Change in Net Position	16,463	13,773
Net Position, Beginning of Year	<u>172,880</u>	<u>159,107</u>
Net Position, End of Year	<u>\$ 189,343</u>	<u>\$ 172,880</u>

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Statements of Cash Flows

Years Ended June 30, 2013 and 2012

(In thousands)

	2013	2012
Operating Activities		
Interest received on loans	\$ 3,167	\$ 2,936
Interest received (paid) on investments	35	(3)
Loan disbursements	(13,216)	(19,954)
Principal repayments on loans	4,514	3,948
Financing fees	1,566	1,410
Federal grant funds expended	(5,428)	(303)
Cash paid for interest	(1,175)	(660)
Cash paid for program administration	(165)	(145)
Net cash used in operating activities	(10,702)	(12,771)
Noncapital Financing Activities		
Proceeds from bond issuance	-	28,393
Cash paid for cost of issuance on long-term debt	-	(195)
Transfers out	(1,102)	(955)
Nonoperating grants received	18,829	11,206
Net cash provided by noncapital financing activities	17,727	38,449
Investing Activities		
Proceeds from maturities of investments	10,000	-
Purchase of investments	(2,000)	(18,006)
Net cash provided by (used in) investing activities	8,000	(18,006)
Increase in Cash and Cash Equivalents	15,025	7,672
Cash and Cash Equivalents, Beginning of Year	33,616	25,944
Cash and Cash Equivalents, End of Year	\$ 48,641	\$ 33,616
Reconciliation of Operating (Loss) Income to Net Cash Used in Operating Activities		
Operating (loss) income	\$ (1,381)	\$ 3,635
Items not providing operating activities cash flows		
Amortization of bond issuance costs	21	14
Amortization of bond premiums	(435)	(280)
Amortization of deferred financing fees	(165)	(170)
Net depreciation of investments	3	2
Changes in		
Accrued interest receivable	(40)	(44)
Accounts receivable – borrowers	(4)	(34)
Loans receivable	(8,702)	(16,006)
Accounts payable	1	14
Accrued interest payable	-	98
Net cash used in operating activities	\$ (10,702)	\$ (12,771)

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

June 30, 2013 and 2012

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

Nature of Operations and Reporting Entity

Act 772 of 1997, as amended, (the Act) authorized the establishment of a fund known as the Safe Drinking Water Fund (the Program), an enterprise fund of the State of Arkansas, to be maintained and administrated by the Arkansas Natural Resources Commission (the Commission or ANRC), formerly known as Arkansas Soil and Water Conservation Commission, and the Arkansas Department of Health. Act 1243 of 2006 authorized the name change to ANRC, which has not had an impact on the Program. The Program is to be capitalized with federal grants, state matching grants, other grants, proceeds of bonds issued by the Arkansas Development Finance Authority (ADFA) or the Commission for the Program and loan repayments utilized to administer the program. These funds may be loaned for water system projects, pledged and used to pay debt service and related costs, used to pay administrative expenses and provide technical assistance for the Program and used for other purposes related to the program.

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, 2013 and 2012, were \$129,000 and \$127,000, respectively.

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.

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

June 30, 2013 and 2012

Recently Issued Accounting Pronouncements

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, 2013 and 2012, cash equivalents of approximately \$48.6 million and \$33.6 million, respectively, consisted of money market mutual funds with variable interest rates. The maturity of the funds is considered to be less than one year because they are redeemable in full immediately.

Investments

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

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

June 30, 2013 and 2012

Bond Issuance Costs and Premiums

Costs related to issuing bonds 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 premiums.

Net Position Restricted for 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.

At June 30, 2013 and 2012, none of the Program's deposits were exposed to custodial credit risk.

Investments

Arkansas statutes authorize 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.

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements June 30, 2013 and 2012

At June 30, 2013 and 2012, the Program had the following investments and maturities:

(In thousands)

Type	June 30, 2013				
	Fair Value	Maturities in Years			
		Less than 1	1-5	6-10	More than 10
U. S. Treasury obligations	\$ 5,001	\$ 5,001	\$ -	\$ -	\$ -
U. S. agencies obligations	5,000	5,000	-	-	-
Money market mutual funds	<u>48,641</u>	<u>48,641</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 58,642</u>	<u>\$ 58,642</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

(In thousands)

Type	June 30, 2012				
	Fair Value	Maturities in Years			
		Less than 1	1-5	6-10	More than 10
U. S. Treasury obligations	\$ 5,006	\$ -	\$ 5,006	\$ -	\$ -
U. S. agencies obligations	12,998	10,000	2,998	-	-
Money market mutual funds	<u>33,616</u>	<u>33,616</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 51,620</u>	<u>\$ 43,616</u>	<u>\$ 8,004</u>	<u>\$ -</u>	<u>\$ -</u>

Interest Rate Risk—As a means of limiting its exposure to fair value losses due to rising interest rates, the Program limits the maturity of investments 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 “Aaa” by Moody’s Investment Service, when owned, and its investments in money market mutual funds, or the investments of those funds were rated “AAAm” or “AAA” by Standard & Poor’s and “Aaa-mf” or “Aaa” by Moody’s Investors Service.

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

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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	\$ 3,000	5%

Summary of Carrying Values

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

<i>(In thousands)</i>	<u>2013</u>	<u>2012</u>
Carrying value		
Investments	\$ <u>58,642</u>	\$ <u>51,620</u>
Included in the following statement of net position captions		
Cash and cash equivalents	\$ 48,641	\$ 33,616
Investments – current portion	10,001	10,000
Investments – restricted	<u>-</u>	<u>8,004</u>
	<u>\$ 58,642</u>	<u>\$ 51,620</u>

Note 3: Loans Receivable

The Program originates loans with Arkansas municipalities for financing the construction of drinking water treatment facilities. These loans are payable in semi-annual installments. At June 30, 2013 and 2012, such loans had a carrying value of approximately \$160.3 million and \$151.6 million, respectively. The loans bear interest at 0.0% to 2.90% and are collateralized by special assessments, user charges or sales and use tax bonds issued by the municipalities.

In fiscal year 2010, the Program began funding loans with American Recovery and Reinvestment Act (ARRA) federal funds. As of June 30, 2013, the Program cumulatively with ARRA and other funding sources had funded \$43.5 million in ARRA loans.

Through the years ended June 30, 2013 and 2012, approximately \$213.1 million and \$210.9 million in loans, respectively, had cumulatively been approved for funding. At June 30, 2013 and 2012, approximately \$27.7 million and \$40.6 million, respectively, remained encumbered and awaiting disbursement to loan recipients.

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements June 30, 2013 and 2012

Note 4: Bonds Payable

Bonds payable were as follows at June 30:

(In thousands)

Series	Interest Rate Range	Final Maturity Dates	2013	2012
2011-C Serial	3.25% – 5.00%	6/1/2026	\$ 24,375	\$ 24,375
	Unamortized premiums		<u>3,302</u>	<u>3,737</u>
			<u>\$ 27,677</u>	<u>\$ 28,112</u>

Activity in bonds payable for 2013 was as follows:

<i>(In thousands)</i>	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due within One Year
2011-C	\$ <u>24,375</u>	\$ <u>-</u>	\$ <u>-</u>	\$ <u>24,375</u>	\$ <u>1,000</u>

The principal amount shown above differs from the amount on the statement of net position due to unamortized premiums of approximately \$3.3 million.

Activity in bonds payable for 2012 was as follows:

<i>(In thousands)</i>	Beginning Balance	Additions	Reductions	Ending Balance	Amount Due within One Year
2011-C	\$ <u>-</u>	\$ <u>24,375</u>	\$ <u>-</u>	\$ <u>24,375</u>	\$ <u>-</u>

The principal amount shown above differs from the amount on the statement of net position due to unamortized premiums of approximately \$3.7 million.

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

June 30, 2013 and 2012

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

<i>(In thousands)</i>	Principal	Interest
Fiscal Year ending June 30,		
2014	\$ 1,000	\$ 1,175
2015	1,385	1,125
2016	1,470	1,056
2017	1,565	983
2018	1,660	905
2019 – 2023	9,975	3,169
2024 – 2026	7,320	607
	24,375	9,020
Unamortized premiums	3,302	-
	\$ 27,677	\$ 9,020

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

In the prior 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 is a combined issue between the Program and the State of Arkansas Construction Assistance Revolving Loan Fund Program. This issue offers 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 is \$28.1 million, net of unamortized premiums.

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 is economically dependent upon revenue from the Environmental Protection Agency (EPA). During 2013 and 2012, the Program received approximately 79% and 71%, respectively, of total revenue in the form of federal grants. The Program has fully disbursed all ARRA federal funds.

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

June 30, 2013 and 2012

Program Set Asides

As shown in the supplemental information, the Program has five set aside funds. These set aside funds make up 31% of the annual capitalization grant awarded each year. These funds are used to provide for reimbursement of expenses of the Program. Section 1452 of the EPA Federal Guidelines for the Implementation of Drinking Water State Revolving Loan Fund indicates a state may reserve the right to redirect unused set aside funds as eligible expenditures of the Program. Since the inception of the Program, ANRC, in conjunction with DOH, has redirected approximately \$6.3 million from previous years' capitalization grants as eligible funds for disbursement to loan borrowers.

Principal Forgiveness Loans

In fiscal year 2012, the Program began funding principal forgiveness loans (PF) with Base federal 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 and 2013 grants. 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	Base Capitalization Grant Award	PF Minimum Amount	PF Maximum Amount	Cumulative Disbursements	PF Remaining to Disburse
2010	\$ 20,539	\$ 6,162	\$ 20,539	\$ 4,758	\$ 1,404
2011	14,252	4,276	14,252	409	3,867
2012	13,582	2,716	4,075	439	2,277
2013	12,743	2,549	3,823	-	2,549
Totals				\$ 5,606	\$ 10,097

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

Notes to Financial Statements

June 30, 2013 and 2012

The Program has allocated the minimum amount from each Base Capitalization grant for principal forgiveness loans. The Program forgives the loans as the construction draws are disbursed. In fiscal year 2013, \$5.4 million in principal forgiveness loans have been expensed.

Contingency

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 at June 30, 2013 and 2012, 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 Safe Drinking Water
Revolving Loan Fund Program
Combining Statement of Net Position
June 30, 2013**

<i>(In thousands)</i>	Small System Technical Assistance	Well Head Protection	Capacity Development	State Program Management
Current Assets				
Cash and cash equivalents	\$ -	\$ -	\$ -	\$ -
Accrued interest receivable	-	-	-	-
Accounts receivable – borrowers	-	-	-	-
Accounts receivable – EPA	-	64	161	111
Investments – current portion	-	-	-	-
Total current assets	<u>-</u>	<u>64</u>	<u>161</u>	<u>111</u>
Noncurrent Assets				
Loans receivable – restricted				
Construction	-	-	-	-
Northeast Arkansas Public Water Authority	-	-	-	-
Other assets	-	-	-	-
Total noncurrent assets	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total assets	<u>-</u>	<u>64</u>	<u>161</u>	<u>111</u>
Current Liabilities				
Accounts payable	\$ -	\$ 64	\$ 161	\$ 111
Accrued interest payable	-	-	-	-
Bonds payable – current portion	-	-	-	-
Total current liabilities	<u>-</u>	<u>64</u>	<u>161</u>	<u>111</u>
Noncurrent Liabilities				
Bonds payable, net of unamortized premiums	-	-	-	-
Deferred fees	-	-	-	-
Total noncurrent liabilities	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total liabilities	<u>-</u>	<u>64</u>	<u>161</u>	<u>111</u>
Net Position				
Restricted for program requirements	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Fees and Expenses	Revolving Loan Fund	Total
\$ 5,948	\$ 42,693	\$ 48,641
3	277	280
151	-	151
117	-	453
<u>-</u>	<u>10,001</u>	<u>10,001</u>
<u>6,219</u>	<u>52,971</u>	<u>59,526</u>
-	156,273	156,273
4,063	-	4,063
<u>-</u>	<u>160</u>	<u>160</u>
<u>4,063</u>	<u>156,433</u>	<u>160,496</u>
<u>10,282</u>	<u>209,404</u>	<u>220,022</u>
\$ 128	\$ -	\$ 464
-	98	98
<u>-</u>	<u>1,000</u>	<u>1,000</u>
<u>128</u>	<u>1,098</u>	<u>1,562</u>
-	26,677	26,677
<u>2,440</u>	<u>-</u>	<u>2,440</u>
<u>2,440</u>	<u>26,677</u>	<u>29,117</u>
<u>2,568</u>	<u>27,775</u>	<u>30,679</u>
<u>\$ 7,714</u>	<u>\$ 181,629</u>	<u>\$ 189,343</u>

State of Arkansas Safe Drinking Water Revolving Loan Fund Program

**Combining Statement of Revenues, Expenses and Changes in Net Position
Year Ended June 30, 2013**

<i>(In thousands)</i>	Small System Technical Assistance	Well Head Protection	Capacity Development	State Program Management
Operating Revenues				
Interest on investments	\$ -	\$ -	\$ -	\$ -
Interest on loans	-	-	-	-
Financing fees	-	-	-	-
Net depreciation of investments	-	-	-	-
Total operating revenues	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Operating Expenses				
Program administration	-	-	-	-
Federal financial assistance				
Base federal grant	-	-	-	-
Bond interest	-	-	-	-
Amortization of bond issuance costs	-	-	-	-
Amortization of bond premiums	-	-	-	-
Total operating expenses	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Operating Income (Loss)	-	-	-	-
Nonoperating Revenue				
Base federal grants	<u>8</u>	<u>773</u>	<u>1,880</u>	<u>1,027</u>
Total nonoperating revenue	<u>8</u>	<u>773</u>	<u>1,880</u>	<u>1,027</u>
Income Before Transfers (Out) In, Net	8	773	1,880	1,027
Transfers (Out) In, Net	<u>(8)</u>	<u>(773)</u>	<u>(1,880)</u>	<u>(1,027)</u>
Change in Net Position	-	-	-	-
Net Position, Beginning of Year	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Net Position, End of Year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Fees and Expenses	Revolving Loan Fund	Total
\$ -	\$ 39	\$ 39
82	3,121	3,203
1,736	-	1,736
<u>-</u>	<u>(3)</u>	<u>(3)</u>
<u>1,818</u>	<u>3,157</u>	<u>4,975</u>
167	-	167
-	5,428	5,428
-	1,175	1,175
-	21	21
<u>-</u>	<u>(435)</u>	<u>(435)</u>
<u>167</u>	<u>6,189</u>	<u>6,356</u>
1,651	(3,032)	(1,381)
<u>1,595</u>	<u>13,624</u>	<u>18,907</u>
<u>1,595</u>	<u>13,624</u>	<u>18,907</u>
3,246	10,592	17,526
<u>1,912</u>	<u>713</u>	<u>(1,063)</u>
5,158	11,305	16,463
<u>2,556</u>	<u>170,324</u>	<u>172,880</u>
<u>\$ 7,714</u>	<u>\$ 181,629</u>	<u>\$ 189,343</u>

**State of Arkansas Safe Drinking Water
Revolving Loan Fund Program
Combining Statement of Cash Flows
Year Ended June 30, 2013**

<i>(In thousands)</i>	Small System Technical Assistance	Well Head Protection	Capacity Development
Operating Activities			
Interest received on loans	\$ -	\$ -	\$ -
Interest received on investments	-	-	-
Loan disbursements	-	-	-
Principal repayments on loans	-	-	-
Financing fees	-	-	-
Federal grant funds expended	-	-	-
Cash paid for interest	-	-	-
Cash paid for program administration	-	-	-
	<hr/>	<hr/>	<hr/>
Net cash provided by (used in) operating activities	-	-	-
Noncapital Financing Activities			
Transfers (out) in	(9)	(782)	(1,887)
Nonoperating grants received	9	782	1,887
	<hr/>	<hr/>	<hr/>
Net cash provided by noncapital financing activities	-	-	-
Investing Activities			
Proceed from maturities of investments	-	-	-
Purchase of investments	-	-	-
	<hr/>	<hr/>	<hr/>
Net cash provided by investing activities	-	-	-
Increase in Cash and Cash Equivalents	-	-	-
Cash and Cash Equivalents, Beginning of Year	<hr/>	<hr/>	<hr/>
Cash and Cash Equivalents, End of Year	\$ <hr/>	\$ <hr/>	\$ <hr/>
Reconciliation of Operating Income (Loss) to Net Cash Provided By (Used In) Operating Activities			
Operating income (loss)	\$ -	\$ -	\$ -
Item not providing operating activities cash flows			
Amortization of bond issuance costs	-	-	-
Amortization of bond premiums	-	-	-
Amortization of deferred financing fees	-	-	-
Net depreciation of investments	-	-	-
Changes in			
Accrued interest receivable	-	-	-
Accounts receivable - borrowers	-	-	-
Loans receivable	-	-	-
Accounts payable	-	-	-
	<hr/>	<hr/>	<hr/>
Net cash provided by (used in) operating activities	\$ <hr/>	\$ <hr/>	\$ <hr/>

State Program Management	Fees and Expense	Revolving Loan Fund	Total
\$ -	\$ 96	\$ 3,071	\$ 3,167
-	-	35	35
-	-	(13,216)	(13,216)
-	58	4,456	4,514
-	1,552	14	1,566
-	-	(5,428)	(5,428)
-	-	(1,175)	(1,175)
-	(165)	-	(165)
-	1,541	(12,243)	(10,702)
(1,050)	1,913	713	(1,102)
1,050	1,477	13,624	18,829
-	3,390	14,337	17,727
-	-	10,000	10,000
-	-	(2,000)	(2,000)
-	-	8,000	8,000
-	4,931	10,094	15,025
-	1,017	32,599	33,616
\$ -	\$ 5,948	\$ 42,693	\$ 48,641
\$ -	\$ 1,651	\$ (3,032)	\$ (1,381)
-	-	21	21
-	-	(435)	(435)
-	(165)	-	(165)
-	-	3	3
-	15	(55)	(40)
-	(18)	14	(4)
-	57	(8,759)	(8,702)
-	1	-	1
\$ -	\$ 1,541	\$ (12,243)	\$ (10,702)