

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

June 30, 2020 and 2019

**Combined Financial Statements
And
Supplementary Information**

With

Independent Auditor's Report



FROST, PLLC
Certified Public Accountants

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Independent Auditor's Report

Commissioners of the Arkansas Natural
Resources Commission

Board of Directors
Arkansas Development Finance Authority
Little Rock, Arkansas

Report on the Combined Financial Statements

We have audited the accompanying combined financial statements of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program, which comprise the combined statements of net position as of June 30, 2020 and 2019, and the related combined statements of revenues, expenses and changes in net position, and cash flows for the years then ended and the related notes to the combined financial statements.

Management's Responsibility for the Combined Financial Statements

Management is responsible for the preparation and fair presentation of these combined 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 combined financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these combined 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 audits to obtain reasonable assurance about whether the combined financial statements are free from material misstatement.

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

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

Opinions

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program as of June 30, 2020 and 2019, 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 Matter

As discussed in Note 1.a., the accompanying combined financial statements present only the State of Arkansas Safe Drinking Water Revolving Loan Fund Program and do not purport to, and do not, present fairly the financial position of the State of Arkansas as of June 30, 2020 and 2019, 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. 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 information on pages 4 through 8 be presented to supplement the basic combined financial statements. Such information, although not a part of the basic combined 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 combined 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 combined financial statements, and other knowledge we obtained during our audits of the basic combined financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the combined financial statements that collectively comprise the State of Arkansas Safe Drinking Water Revolving Loan Fund Program's basic combined financial statements. The schedule of expenditures of federal awards, as required by the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards*, is presented for purposes of additional analysis and is not a required part of the basic combined financial statements.

The supplementary information on pages 24 through 26 and the schedule of expenditures of federal awards on page 33 are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic combined financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic combined 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 combined financial statements or to the basic combined financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic combined 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 November 2, 2020, on our consideration of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program's 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 Arkansas Development Finance Authority's internal control over financial reporting and compliance.

Frost, PLLC

Certified Public Accountants

Little Rock, Arkansas
November 2, 2020

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Management's Discussion and Analysis

For the Years Ended June 30, 2020 and 2019

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 combined financial statements and notes as a whole, which follow this section of the report.

Discussion of Combined Financial Statements

The June 30, 2020 basic combined financial statements include three required statements: the combined statement of net position; the combined statement of revenues, expenses and changes in net position; and the combined statement of cash flows. Comparative totals as of and for the years ended June 30, 2019 and 2018 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 Combined 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 – Combined Statements of Net Position

	<u>2020</u>	<u>2019</u>	<u>2018</u>
<i>(In thousands)</i>			
Total assets	<u>\$ 298,016</u>	<u>\$ 276,517</u>	<u>\$ 264,937</u>
Liabilities			
Current liabilities	2,446	2,621	2,741
Noncurrent liabilities	<u>11,951</u>	<u>14,185</u>	<u>16,539</u>
Total liabilities	<u>14,397</u>	<u>16,806</u>	<u>19,280</u>
Net position			
Restricted by bond resolution and Program requirements	<u>\$ 283,619</u>	<u>\$ 259,711</u>	<u>\$ 245,657</u>

The Program's total assets have continually increased over the past three years. At June 30, 2020, total assets increased \$21.5 million from June 30, 2019 which is primarily attributable to the increase in cash and cash equivalents and loans receivable – restricted, which is offset by the decrease in current portion of investments. At June 30, 2019, total assets increased \$11.6 million from June 30, 2018, which was attributable to an increase in total investments.

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Management’s Discussion and Analysis (cont.)

For the Years Ended June 30, 2020 and 2019

The following table reports loan activity for each year:

	<u>2020</u>	<u>2019</u>	<u>2018</u>
<i>(In thousands)</i>			
Loan disbursements	\$ 30,417	\$ 10,377	\$ 4,328
Loan repayments	<u>15,776</u>	<u>10,039</u>	<u>9,052</u>
Net increase (decrease) in loans receivable	<u>\$ 14,641</u>	<u>\$ 338</u>	<u>\$ (4,724)</u>

Grants from the Environmental Protection Agency (“EPA”) comprised 49%, 41% and 3% of the funding source of the repayable loan disbursements for fiscal years ended June 30, 2020, 2019 and 2018, respectively. Per EPA guidelines, federal grants are allocated between repayable and principal forgiveness loans and administrative costs. Depending on funds available, the amount funded from EPA base federal grants will fluctuate. At June 30, 2020, the Program had \$12.1 million available to fund repayable and principal forgiveness loans. The table below reflects the amounts used from each funding source for fiscal years 2020, 2019 and 2018 as follows:

	<u>2020</u>	<u>2019</u>	<u>2018</u>
<i>(In thousands)</i>			
EPA federal base	\$ 14,844	\$ 4,256	\$ 137
Revolving Program funds	12,262	1,903	-
State matching funds	<u>3,311</u>	<u>4,218</u>	<u>4,191</u>
	<u>\$ 30,417</u>	<u>\$ 10,377</u>	<u>\$ 4,328</u>

The Program utilized EPA federal grants to fund loans, along with other funding sources. The Program’s loan activity has begun to increase with the funding of several water meter projects to municipalities, water user associations and public facilities boards. The Program has several funding sources to meet the increasing loan activity.

The Program’s loan repayments have increased over the past three years, which consists of the scheduled loan repayments and loan prepayments. The Program received prepayment totaling \$5.1 million from non-pledged loans in 2020. In fiscal year 2019, the Program did not receive any prepayment funds. Prepayments are either from loans pledged to a bond issue or non-pledged loans. The Program’s general bond resolution allows the Program to use loan prepayments to make new loans within 90 days of receipt, pay principal and interest at debt service or pay principal and interest on called bonds. The Program has chosen to use prepayments from pledged loans to pay scheduled debt service payments. Any prepayments from non-pledged loans are available to be used for the Program’s purpose.

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Management's Discussion and Analysis (cont.)

For the Years Ended June 30, 2020 and 2019

The Program maintains liquidity for funding loans. The Program invested excess funds in money market mutual funds, U. S. Treasury obligations, U.S. agency obligations and the State Treasurer Money Management Trust Fund ("MMTF") from time to time to allow for re-evaluation of the Program's liquidity needs. The MMTF has a rate of return higher than a money market mutual fund and the funds are available within one business days' notice. The money market mutual funds rates have declined in March 2020 due to the coronavirus pandemic. The Program is evaluating its liquidity needs and investment options. The Program's U. S. agency obligations and U. S. Treasury obligations matured in September 2019 and January 2020, respectively.

The Program's total liabilities decreased to \$14.4 million at June 30, 2020 from \$16.8 million at June 30, 2019 and \$19.3 million at June 30, 2018. In fiscal years 2020 and 2019, the Program had a decline of \$2.3 million and \$2.5 million, respectively, in the bonds payable mainly due to the payment of scheduled bond redemptions.

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

	<u>2020</u>	<u>2019</u>	<u>2018</u>
<i>(In thousands)</i>			
Operating revenues			
Total interest income	\$ 4,062	\$ 4,968	\$ 4,295
Other income	<u>2,038</u>	<u>2,199</u>	<u>1,350</u>
Total operating revenues	<u>6,100</u>	<u>7,167</u>	<u>5,645</u>
Operating expenses			
Program administration	180	171	173
Federal financial assistance	2,590	5,392	5,672
Bond interest	694	804	893
Amortization of bond premiums	<u>(249)</u>	<u>(288)</u>	<u>(321)</u>
Total operating expenses	<u>3,215</u>	<u>6,079</u>	<u>6,417</u>
Operating (loss) income	2,885	1,088	(772)
Base federal grants	21,311	13,357	9,729
Transfers out	<u>(288)</u>	<u>(391)</u>	<u>(3,960)</u>
Changes in net position	23,908	14,054	4,997
Net position - beginning of year	<u>259,711</u>	<u>245,657</u>	<u>240,660</u>
Net position - end of year	<u>\$ 283,619</u>	<u>\$ 259,711</u>	<u>\$ 245,657</u>

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Management's Discussion and Analysis (cont.)

For the Years Ended June 30, 2020 and 2019

Total interest income has fluctuated over the past three years. Included in total interest income is interest earned on loans and interest earned on investments, which has decreased to \$4.1 million at June 30, 2020, increased to \$5.0 million for the year ended June 30, 2019 and decreased to \$4.3 million for the year ended June 30, 2018. The decline in fiscal year 2020 was due to the decline of interest earned on investments of \$849,000. The Program invested funds in money market mutual funds and MMTF. The decline was due to the Fed fund rate decline in March 2020 due to the coronavirus pandemic. This has had an impact on interest earnings of the Program. The Program monitors its investments and earnings to provide additional income for the Program. In fiscal year 2019, interest on investments increased \$685,000, which was attributable to the increase in the MMTF interest rate. At fiscal year-ends 2020 and 2019, the MMTF interest rate was 0.51% and 2.74%, respectively. The Program considers the \$106.7 million in MMTF as cash and cash equivalents. These funds yield a slightly higher rate of return than the Program's other money market mutual fund rates. The average yield on cash, cash equivalents and investments for fiscal year 2020 has decreased to 1.09%; whereas the average yields for fiscal years 2019 and 2018 were 1.75% and 1.28%, respectively.

The interest on loans has decreased by \$57,000 and \$13,000 for fiscal years 2020 and 2019, respectively. The Program is continuously making loans with interest rates between 0.00% and 2.90%. The average return on loans is 1.65%, 1.75% and 1.73% for the fiscal years 2020, 2019 and 2018, respectively.

Other income includes financing fee income and the net appreciation of investments. In the current fiscal year, other income decreased \$161,000 due to a decrease in net appreciation of investments of \$187,000 which is offset by an increase in financing fee income of \$26,000. In the prior fiscal year, the Program had an increase of \$849,000 in other income, which consists of the increase in the appreciation of investments of \$834,000 and financing fee income of \$14,000. Net appreciation of investments is the change in market value of the portfolio. Financing fee represents the up 1% fee charged on the outstanding loan balance.

Total operating expenses have decreased over the past three years to \$3.2 million for the year ended June 30, 2020 from \$6.1 million for the year ended June 30, 2019 and \$6.4 million for the year ended June 30, 2018. The decline in fiscal year 2020 and 2019 is attributed to the decline of federal financial assistance and bond interest expense. 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. The Program is required by state law to use only federal grant funds to make principal forgiveness loans. For the years ended June 30, 2020 and 2019, the Program has awarded principal forgiveness loans to multiple borrowers and has forgiven \$2.6 million and \$5.4 million, respectively. The Federal financial assistance is based upon the loans available to be funded and the rate at which the borrower completes their project.

Federal grant revenue increased \$8.0 million for fiscal year 2020, which comprises of draws for loans and administrative expenses. Federal grant revenue for construction draws increased \$7.8 million and \$3.8 million in fiscal years 2020 and 2019, respectively. Arkansas Natural Resources Commission ("ANRC") and Arkansas Department of Health ("DOH") incur administration expenses and are reimbursed using federal grant revenue for administering the Program. The Program primarily used federal grants for funding loans and paying expenses. These funds were drawn down from the federal government as the municipalities, ANRC or DOH, incurred expenses.

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Management's Discussion and Analysis (cont.)

For the Years Ended June 30, 2020 and 2019

For the fiscal years 2020 and 2019, the Program's transfers out, net were \$288,000 and \$391,000, respectively. As funds are available, the Program receives transfers in from the ANRC Water, Waste Disposal and Pollution Abatement Facilities General Obligation Bond Fund Program, which represents the state matching funds for the Program. Transfers out are transfers to state agencies for Program administration expenses. The details of transfers in and out are presented in the following table:

	<u>2020</u>	<u>2019</u>	<u>2018</u>
<i>(In thousands)</i>			
ANRC - state match	\$ 3,311	\$ 3,342	\$ -
DOH	(3,149)	(3,158)	(3,410)
ANRC - administration	<u>(450)</u>	<u>(575)</u>	<u>(550)</u>
Transfers out, net	<u>\$ (288)</u>	<u>\$ (391)</u>	<u>\$ (3,960)</u>

The net position of the Program increased \$38.0 million in the past two years. The bond resolution and the Program guidelines 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 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 Arkansas Department of Finance Authority's Chief Financial Officer by telephoning 501.682.5900 or by contacting the ANRC Water Development Division Chief at 501.682.1611.

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Combined Statements of Net Position

June 30, 2020 and 2019

(In Thousands)

<u>Assets</u>	<u>2020</u>	<u>2019</u>
Current assets		
Cash and cash equivalents	\$ 125,908	\$ 73,272
Accrued interest receivable		
Investments	38	171
Loans	83	39
Accounts receivable		
Borrowers	66	24
Environmental Protection Agency	311	437
Receivable from other funds	-	54
Investments	-	45,551
Total current assets	<u>126,406</u>	<u>119,548</u>
Noncurrent assets		
Loans - restricted		
Construction	171,610	153,476
Northeast Arkansas Public Water Authority	-	3,493
Total noncurrent assets	<u>171,610</u>	<u>156,969</u>
Total assets	<u>298,016</u>	<u>276,517</u>
 <u>Liabilities and Net Position</u> 		
Current liabilities		
Accounts payable	411	444
Payable to other funds	-	54
Accrued interest payable	50	58
Current portion of bonds payable	1,985	2,065
Total current liabilities	<u>2,446</u>	<u>2,621</u>
Noncurrent liabilities		
Bonds payable, net of unamortized premiums	<u>11,951</u>	<u>14,185</u>
Total liabilities	<u>14,397</u>	<u>16,806</u>
Net position		
Restricted by bond resolution, enabling legislation and Program requirements	<u>\$ 283,619</u>	<u>\$ 259,711</u>

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

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Combined Statements of Revenues, Expenses and Changes in Net Position

For the Years Ended June 30, 2020 and 2019

(In Thousands)

	<u>2020</u>	<u>2019</u>
Operating revenues		
Interest on investments	\$ 1,380	\$ 2,229
Interest on loans	2,682	2,739
Financing fee income	1,583	1,557
Net appreciation of investments	455	642
Total operating revenues	6,100	7,167
Operating expenses		
Program administration	180	171
Federal financial assistance - base federal grants	2,590	5,392
Bond interest	694	804
Amortization of bond premiums	(249)	(288)
Total operating expenses	3,215	6,079
Operating income	2,885	1,088
Nonoperating revenues		
Base federal grants	21,311	13,357
Income before transfers out, net	24,196	14,445
Transfers out, net	(288)	(391)
Change in net position	23,908	14,054
Net position - beginning of year	259,711	245,657
Net position - end of year	\$ 283,619	\$ 259,711

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

**STATE OF ARKANSAS SAFE DRINKING WATER
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Combined Statements of Cash Flows

For the Years Ended June 30, 2020 and 2019

(In Thousands)

	<u>2020</u>	<u>2019</u>
Cash flows from operating activities		
Financing fee income received	\$ 1,489	\$ 1,605
Cash paid for program administration	<u>(192)</u>	<u>(150)</u>
Net cash provided by operating activities	<u>1,297</u>	<u>1,455</u>
Cash flows from noncapital financing activities		
Repayments of long-term debt	(2,065)	(2,205)
Cash paid for interest	(702)	(812)
Transfers out	(308)	(437)
Nonoperating grants received	<u>21,437</u>	<u>13,479</u>
Net cash provided by noncapital financing activities	<u>18,362</u>	<u>10,025</u>
Cash flows from investing activities		
Interest received on investments	1,513	2,273
Interest received on loans	2,689	2,680
Principal repayments on loans	15,776	10,039
Loan disbursements	(30,417)	(10,377)
Federal grant funds expended	(2,590)	(5,392)
Proceeds from maturities of investments	46,006	29,961
Purchase of investments	<u>-</u>	<u>(40,982)</u>
Net cash provided (used) by investing activities	<u>32,977</u>	<u>(11,798)</u>
Net increase (decrease) in cash and cash equivalents	52,636	(318)
Cash and cash equivalents - beginning of year	<u>73,272</u>	<u>73,590</u>
Cash and cash equivalents - end of year	<u>\$ 125,908</u>	<u>\$ 73,272</u>

	<u>2020</u>	<u>2019</u>
Reconciliation of changes in net assets to net cash provided by operating activities		
Operating income	\$ 2,885	\$ 1,088
Adjustments to reconcile operating income of changes in net assets to net cash provided by operating activities		
Interest on investments	(1,380)	(2,229)
Interest on loans	(2,682)	(2,739)
Bond interest	694	804
Amortization of bond premiums	(249)	(288)
Net appreciation of investments	(455)	(642)
Federal grants expended	2,590	5,392
Changes in operating assets and liabilities		
Accounts receivable - borrowers	(42)	(5)
Due to/from other funds	(54)	54
Accounts payable	<u>(10)</u>	<u>20</u>
Net cash provided by operating activities	<u>\$ 1,297</u>	<u>\$ 1,455</u>

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

**STATE OF ARKANSAS SAFE DRINKING WATER
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Notes to Combined Financial Statements

June 30, 2020 and 2019

1. Nature of Operations and Summary of Significant Accounting Policies

- a. **Nature of operations and reporting entity** – Act 772 of 1997, as amended, 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 (“ANRC”). Effective July 1, 2019, ANRC is a division of the Arkansas Department of Agriculture and is still the lead agency for 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 ANRC for the Program and loan repayments utilized to administer the program. Effective July 1, 2019, ADFA is a division of the Arkansas Department of Commerce. These funds may be loaned for water system projects, pledged and used to pay debt service and related costs, used to, and are included to, pay the Program’s 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 combined 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 were \$132,000 and \$123,000 for the years ended June 30, 2020 and 2019, respectively, and are included in the Program’s administration expenses.

- b. **Use of estimates** – The preparation of combined 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 combined 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.
- c. **Measurement focus and basis of accounting** – 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 combined statements 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**

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Notes to Combined Financial Statements

June 30, 2020 and 2019

1. Nature of Operations and Summary of Significant Accounting Policies (cont.)

- d. **Recently issued accounting pronouncements** – Governmental Accounting Standards Board (“GASB”) Statement No. 87, “Leases.” This statement establishes a new single model for lease accounting based on the principle that leases represent the financing of the right to use an underlying asset. The effective date is for periods beginning after June 15, 2021. During fiscal year 2020, the Program implemented GASB Statement No. 87, which did not have a material impact on its combined financial statements.

GASB Statement No. 89, “Accounting for Interest Cost Incurred before the End of a Construction Period.” This statement enhances the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and simplifies accounting for interest cost incurred before the end of a construction period. This statement requires that interest cost incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. This statement supersedes paragraphs 5 through 22 of GASB Statement No. 62, “Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.” This statement is effective for periods beginning after December 15, 2020. The requirements of this statement should be applied prospectively. During fiscal year 2020, the Program implemented GASB Statement No. 89, which did not have a material impact on its combined financial statements.

GASB Statement No. 93, “Replacement of Interbank Offered Rates.” This statement will enhance comparability of accounting and financial reporting requirements and will improve the consistency of authoritative literature. More comparable reporting will improve the usefulness of information for users of state and local government financial statements. The removal of the London Interbank Offered Rate as an appropriate benchmark interest rate is effective for reporting periods ending after December 31, 2021. All other requirements of this statement are effective for reporting periods beginning after June 15, 2020. Earlier application is encouraged. The Program has not determined the impact, if any, that this statement could have on its financial statements.

- e. **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, 2020 and 2019, cash equivalents of approximately \$125.9 million and \$73.3 million, respectively, consisted of money market mutual funds with variable interest rates and an internal governmental investment pool administrated by the State of Arkansas. The maturity of the funds is considered to be less than one year because they are redeemable in full immediately.
- f. **Investments** – Investments are carried at fair value. Fair value is determined using quoted market prices. Investment income is related to interest earned on cash and cash equivalents and investments.
- g. **Bond premiums** – Premiums on the sale 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 the premiums.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

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Notes to Combined Financial Statements

June 30, 2020 and 2019

1. Nature of Operations and Summary of Significant Accounting Policies (cont.)

- h. **Financing fees** – The Program receives up to a 1% annual financing fee from borrowers as part of their monthly payment.
- i. **Net position restricted by bond resolution, enabling legislation and program requirements** – Net position restricted by bond resolution, enabling legislation and program requirements represent funds restricted due to the specific provisions of the Program.
- j. **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.

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.

At June 30, 2020 and 2019, 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 Combined Financial Statements

June 30, 2020 and 2019

2. Deposits and Investments (cont.)

At June 30, 2020 and 2019, the Program had the following investments and maturities:

<i>(In thousands)</i>	Maturities in Years				<u>Total</u>
	<u>Less than 1</u>	<u>1 - 5</u>	<u>6 - 10</u>	<u>More than 10</u>	
<u>June 30, 2020</u>					
Money market mutual funds	\$ 19,256	\$ -	\$ -	\$ -	\$ 19,256
State Treasurer Money					
Management Trust Fund	106,652	-	-	-	106,652
	\$ 125,908	\$ -	\$ -	\$ -	\$ 125,908
<u>June 30, 2019</u>					
U.S. agencies obligations	\$ 3,996	\$ -	\$ -	\$ -	\$ 3,996
U.S. Treasury obligations	41,555	-	-	-	41,555
Money market mutual funds	9,759	-	-	-	9,759
State Treasurer Money					
Management Trust Fund	63,513	-	-	-	63,513
	\$ 118,823	\$ -	\$ -	\$ -	\$ 118,823

- a. **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. The Program invests in an internal governmental investment pool administered by the State of Arkansas. The Program may request withdrawal of its funds with one business days’ notice.
- b. **Credit risk** – Credit risk is the risk that the issuer or other counterparty to an investment will not fulfill its obligations. At June 30, 2020, the Program did not have any investments in U. S. agencies obligations. The Program’s 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.
- c. **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:

<u>Issuer</u>	2020		2019	
	<u>Fair Value</u>	<u>Percentage</u>	<u>Fair Value</u>	<u>Percentage</u>
<i>(In thousands)</i>				
State of Arkansas Money				
Management Trust Fund	\$ 106,652	85%	\$ 63,513	53%

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Notes to Combined Financial Statements

June 30, 2020 and 2019

2. Deposits and Investments (cont.)

Summary of Carrying Values

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

	<u>2020</u>	<u>2019</u>
<i>(In thousands)</i>		
Carrying value		
Investments	\$ 125,908	\$ 118,823

Included in the following combined statements of net position captions:

	<u>2020</u>	<u>2019</u>
<i>(In thousands)</i>		
Cash and cash equivalents	\$ 125,908	\$ 73,272
Investments		
Current portion	-	45,551
	<u>\$ 125,908</u>	<u>\$ 118,823</u>

3. Loans Receivable

The Program originates loans with Arkansas municipalities for financing the construction of drinking water treatment facilities. These loans are payable in semiannual installments. At June 30, 2020 and 2019, such loans had a carrying value of approximately \$171.6 million and \$157.0 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 funded loans with American Recovery and Reinvestment Act (“ARRA”) federal funds, along with other funding sources. As of June 30, 2020 and 2019, the Program’s outstanding loan balance for ARRA loans totaled \$17.0 million and \$18.0 million, respectively.

Through the years ended June 30, 2020 and 2019, approximately \$308.7 million and \$253.7 million, respectively, in loans had cumulatively been approved for funding. At June 30, 2020 and 2019, approximately \$28.0 million and \$5.9 million, respectively, remained encumbered and awaiting disbursement to loan recipients.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Notes to Combined Financial Statements

June 30, 2020 and 2019

4. Bonds Payable

Bonds payable consist of the following:

<u>Series</u>	<u>Interest Rate Range</u>	<u>Final Maturity Dates</u>	<u>2020</u>	<u>2019</u>
			<u>(In thousands)</u>	
2011-C Serial	3.25% - 5.00%	June 1, 2028	\$ 13,150	\$ 15,215
	Unamortized premiums		<u>786</u>	<u>1,035</u>
			<u>\$ 13,936</u>	<u>\$ 16,250</u>

Activity in bonds payable consists of the following:

<u>(In thousands)</u>	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Amount Due within One Year</u>
<u>June 30, 2020</u>					
2011-C Serial	<u>\$ 15,215</u>	<u>\$ -</u>	<u>\$ (2,065)</u>	<u>\$ 13,150</u>	<u>\$ 1,985</u>
<u>June 30, 2019</u>					
2011-C Serial	<u>\$ 17,420</u>	<u>\$ -</u>	<u>\$ (2,205)</u>	<u>\$ 15,215</u>	<u>\$ 2,065</u>

The principal amount shown above differs from the amount on the combined statements of net position due to unamortized premiums of approximately \$786,000 and \$1.0 million as of June 30, 2020 and 2019, respectively.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Notes to Combined Financial Statements

June 30, 2020 and 2019

4. Bonds Payable (cont.)

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

<u>Fiscal Year Ended June 30,</u>	<u>Principal</u>	<u>Interest</u>
	<i>(In thousands)</i>	
2021	\$ 1,985	\$ 599
2022	1,900	500
2023	1,900	405
2024	1,900	310
2025	1,875	215
2026-2028	3,590	208
	13,150	2,237
Unamortized premiums	786	-
	\$ 13,936	\$ 2,237

The Program has not had any new bond issuances in fiscal 2020 nor 2019.

5. Fair Value of Financial Instruments

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of three levels of inputs that may be used to measure fair value:

- **Level I** – Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.
- **Level II** – Quoted prices in markets that are not active or inputs, which are observable, either directly or indirectly, for substantially the full term of the asset or liability.
- **Level III** – Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable (i.e., supported by little or no market activity).

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Notes to Combined Financial Statements

June 30, 2020 and 2019

5. Fair Value of Financial Instruments (cont.)

Recurring Measurements

The following table presents the fair value measurements of assets recognized in the accompanying combined financial statements measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall:

	<u>Fair Value</u>	Quoted Prices in Active Markets for Identical Assets <u>(Level I)</u>	Significant Other Observable Inputs <u>(Level II)</u>	Significant Unobservable Inputs <u>(Level III)</u>
<i>(In thousands)</i>				
<u>June 30, 2020</u>				
State Treasurer Money				
Management Trust Fund	\$ 106,652	\$ -	\$ 106,652	\$ -
<u>June 30, 2019</u>				
U.S. agencies obligations	\$ 3,996	\$ -	\$ 3,996	\$ -
U.S. Treasury obligations	41,555	-	41,555	-
State Treasurer Money				
Management Trust Fund	<u>63,513</u>	<u>-</u>	<u>63,513</u>	<u>-</u>
	<u>\$ 109,064</u>	<u>\$ -</u>	<u>\$ 109,064</u>	<u>\$ -</u>

The following is a description of the valuation methodologies and inputs used for assets measured at fair value on a recurring basis and recognized in the accompanying combined financial statements, as well as the general classification of such assets pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the years ended June 30, 2020 or 2019.

Notes to Combined Financial Statements

June 30, 2020 and 2019

5. **Fair Value of Financial Instruments (cont.)**

Where quoted market prices are available in an active market, securities are classified within Level I of the valuation hierarchy. The Program did not classify any of its investments as Level I at June 30, 2020 nor 2019. Level II securities include U.S. government and federal agencies and the State Treasurer Money Management Trust Fund (“MMTF”). If quoted market prices are not available, then fair values are estimated by an independent third party pricing service using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. For these investments, the inputs used by the pricing service to determine fair value may include one, or a combination of observable inputs such as benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data market research publications. The fair value of MMTF is calculated by the internal governmental investment pool. All these types of the Program’s investments are classified within Level II of the valuation hierarchy. In certain cases where Level I or Level II inputs are not available, securities are classified within Level III of the hierarchy. The Program did not have any Level III securities at June 30, 2020 or 2019.

The fair value amounts in the previous table do not reflect all investments included in the amounts presented in the combined statements of net position. GASB Statement No. 72, “Fair Value Measurement and Application,” provides certain exceptions for money market mutual funds.

6. **Concentrations**

Economic Dependency

The Program is economically dependent upon revenue from the Environmental Protection Agency (“EPA”). During fiscal 2020 and 2019, the Program received approximately 78% and 65%, respectively, of total revenue in the form of federal grants.

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. Through federal regulations, the EPA has allowed states to redirect and reserve set asides as needed to ensure proper management of funds.

Section 1452 of the EPA Federal Guidelines for the Implementation of Drinking Water State Revolving Loan Fund (“DWSRF”) 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, with the caveat that those redirected funds may be reclaimed as set aside funds in future federal grants. The Program has reclaimed \$473,000 of the funds previously redirected. Only the State Program Management and Small System Technical Assistance set asides may be reclaimed in future grant years. All others set asides are not eligible to be reclaimed.

Notes to Combined Financial Statements

June 30, 2020 and 2019

6. Concentrations (cont.)

The Code of Federal Regulations section 40 CFR 3540, regarding the DWSRF, states a state may reserve or “bank” set aside funds at the time of the grant application. The intent is that the authority for a set aside activity from one year can be used in a future year when the amount available in that future year is not enough to accomplish the set aside activity. Each set aside activity has specific eligible costs associated with it. Reserved authority in a set aside activity can only be used for that same set aside activity in the future. For each grant application, the state has to demonstrate to EPA that the funds requested for each set aside activity can be used within a two-year period. If this results in the state having additional authority for that activity that they cannot use within the two-year period, they can reserve that additional authority for some unspecified future grant. The amount of authority reserved for each set aside activity will be reported in the Intended Use Plan (“IUP”) for that fiscal year and every succeeding IUP until the authority is used. When the state wants to use the authority that has been reserved, the state must demonstrate to EPA that all of the authority in the future grant and the additional reserved authority can be expended within the two year period. The management of the Program is aware if future federal capitalization grants are not made available, the reserved authority is lost. Since the inception of the Program, DOH has reserved authority of \$10.1 million in the Small System Technical Assistance and the State Program Management set aside with the caveat that those redirected funds may be reclaimed as set aside funds in future federal grants. The Program has reclaimed \$1.7 million of these set aside funds.

Principal Forgiveness Loans

In fiscal year 2012, the Program began funding principal forgiveness (“PF”) loans 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. The percentage was changed to be not less than 20%, but not greater than 30% of the Federal Fiscal Years 2012 through 2018 grants. Starting with the fiscal year 2019 grants, at least 6%, but not greater than 35%, of the grant must be provided as subsidization be in the form of a loan with principal forgiveness or negative interest to disadvantaged communities.

To be eligible to receive subsidy, the borrower must show either:

1. The current utility rates or proposed utility rates for 4,000 gallons of water on an annual basis are at least 1.5% of the Median Household Income (“MHI”) for the project area.
2. At least 51% of customers who benefit from the project have either low or moderate income as defined by the U.S. Department of Housing and Urban Development’s Community Block Grant Program; and have 1.25% of MHI.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Notes to Combined Financial Statements

June 30, 2020 and 2019

6. Concentrations (cont.)

To be a disadvantaged community, as defined in the annual Intended Use Plan:

1. Have a MHI below that of the State’s MHI. Arkansas’s MHI is the average of the most recent three years of available data on the American Community Survey five-year estimates provided by the University of Arkansas – Little Rock. Arkansas’s MHI for State Fiscal Year 2020 is \$41,657.

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

Federal Fiscal Year	Base Capitalization <u>Grant Award</u>	PF Minimum <u>Amount</u>	PF Maximum <u>Amount</u>	Program Allocation <u>Amount</u>	Cumulative Disbursements	PF Remaining to Disburse
<i>(In thousands)</i>						
2015	\$ 13,445	\$ 2,689	\$ 4,034	\$ 4,034	\$ 3,855	\$ 179
2016	12,719	2,544	6,360	6,360	6,273	87
2017	12,610	2,522	8,601	3,840	1,354	2,486
2018	16,711	3,342	-	4,607	-	4,607
2019	16,555	4,304	-	2,383	<u>48</u>	<u>2,335</u>
					<u>\$ 11,530</u>	<u>\$ 9,694</u>

Any closed grants have been removed from the chart above. In fiscal year 2018, with EPA Region 6 approval, the Program changed its targeted PF to the maximum amount from base capitalization grant starting with the 2011 capitalization grant. The Program forgives the loans as the construction draws are disbursed. The Program established a targeted PF amount for fiscal years 2017 and 2018 grants. The Program will use the minimum amount in fiscal year 2019. In fiscal years 2020 and 2019, the Program expensed \$2.6 million and \$5.4 million in PF loans, respectively. An additional 30% can be allocated for disadvantaged communities.

Since the American Recovery and Reinvestment Act, annual federal appropriations laws have required states to provide a minimum amount of additional subsidization for DWSRF projects. Prior to ARRA, a state could, and still can, establish at its discretion disadvantaged community criteria and provide additional subsidization in the form of PF or negative interest rate loans to a water system that the state designates as serving a disadvantaged community. A state may use those same criteria in determining priority for additional subsidy to a water system as required by annual federal appropriations laws.

A state may use its additional subsidy authority under the disadvantaged community program in combination (additively) with additional subsidy authority provided through annual federal appropriations law. Additional subsidization can take the form of PF (the most commonly used form), negative interest rate loans or grants (except for designated disadvantaged community programs).

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

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Notes to Combined Financial Statements

June 30, 2020 and 2019

6. Concentrations (cont.)

Contingencies

The Program is partially capitalized by state funds and a federal grant program, which are governed by various rules and regulations of the grantor agency. Costs charged to the respective grant programs are subject to audit and adjustments by the grantor agency; therefore, to the extent the Program has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectibility 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 combined financial statements for such a contingency.

Coronavirus Disease 2019 (“COVID-19”)

The COVID-19 outbreak, characterized as a pandemic by the World Health Organization on March 11, 2020, has caused significant disruptions in international and U.S. economies and markets. The Program believes it is taking all reasonable precautions in the management of its operations in response to the COVID-19 pandemic. The duration of these uncertainties and ultimate effect of the value of Program’s investments and operating results cannot be reasonably estimated at this time.

7. Subsequent Events Evaluation Date

The Program evaluated the events and transactions subsequent to its June 30, 2020 combined statement of net position date and determined there were no significant events to report through November 2, 2020, which is the date the Program issued its combined financial statements.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Combining Statement of Net Position

June 30, 2020

(In Thousands)

<u>Assets</u>	<u>Small System Technical Assistance</u>	<u>Well Head Protection</u>
Current assets		
Cash and cash equivalents	\$ -	\$ -
Accrued interest receivable		
Investment	-	-
Loans	-	-
Accounts receivable		
Borrowers	-	-
EPA	-	43
Total current assets	<u>-</u>	<u>43</u>
Noncurrent assets		
Loans receivable - restricted		
Construction	<u>-</u>	<u>-</u>
Total assets	<u>-</u>	<u>43</u>
<u>Liabilities and Net Position</u>		
Current liabilities		
Accounts payable	-	43
Accrued interest payable	-	-
Current portion of bonds payable	<u>-</u>	<u>-</u>
Total current liabilities	<u>-</u>	<u>43</u>
Noncurrent liabilities		
Bonds payable, net of unamortized premiums and current portion	<u>-</u>	<u>-</u>
Total liabilities	<u>-</u>	<u>43</u>
Net position		
Restricted by bond resolution, enabling legislation and Program requirements	<u>\$ -</u>	<u>\$ -</u>

<u>Capacity Development</u>	<u>State Program Management</u>	<u>Fees and Expenses</u>	<u>Revolving Loan Fund</u>	<u>Total</u>
\$ -	\$ -	\$ 10,854	\$ 115,054	\$ 125,908
-	-	1	37	38
-	-	-	83	83
-	-	66	-	66
<u>128</u>	<u>89</u>	<u>51</u>	<u>-</u>	<u>311</u>
128	89	10,972	115,174	126,406
-	-	-	171,610	171,610
<u>128</u>	<u>89</u>	<u>10,972</u>	<u>286,784</u>	<u>298,016</u>
128	89	132	19	411
-	-	-	50	50
-	-	-	1,985	1,985
<u>128</u>	<u>89</u>	<u>132</u>	<u>2,054</u>	<u>2,446</u>
-	-	-	11,951	11,951
<u>128</u>	<u>89</u>	<u>132</u>	<u>14,005</u>	<u>14,397</u>
<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,840</u>	<u>\$ 272,779</u>	<u>\$ 283,619</u>

See independent auditor's report.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Combining Statement of Revenues, Expenses and Changes in Net Position

For the Year Ended June 30, 2020

(In Thousands)

	Small System Technical <u>Assistance</u>	Well Head <u>Protection</u>
Operating revenues		
Interest on investments	\$ -	\$ -
Interest on loans	-	-
Financing fee income	-	-
Net appreciation of investments	<u>-</u>	<u>-</u>
Total operating revenues	<u>-</u>	<u>-</u>
Operating expenses		
Program administration	-	-
Federal financial assistance - base federal grants	-	-
Bond interest	-	-
Amortization of bond premiums	<u>-</u>	<u>-</u>
Total operating expenses	<u>-</u>	<u>-</u>
Operating income	-	-
Nonoperating revenues		
Base federal grants	<u>-</u>	<u>648</u>
Income before transfers (out) in, net	-	648
Transfers (out) in, net	<u>-</u>	<u>(648)</u>
Changes in net position	-	-
Net position - beginning of year	<u>-</u>	<u>-</u>
Net position - end of year	<u><u>\$ -</u></u>	<u><u>\$ -</u></u>

<u>Capacity Development</u>	<u>State Program Management</u>	<u>Fees and Expenses</u>	<u>Revolving Loan Fund</u>	<u>Total</u>
\$ -	\$ -	\$ 94	\$ 1,286	\$ 1,380
-	-	49	2,633	2,682
-	-	1,583	-	1,583
-	-	-	455	455
-	-	1,726	4,374	6,100
-	-	180	-	180
-	-	-	2,590	2,590
-	-	-	694	694
-	-	-	(249)	(249)
-	-	180	3,035	3,215
-	-	1,546	1,339	2,885
1,560	940	729	17,434	21,311
1,560	940	2,275	18,773	24,196
(1,560)	(940)	(451)	3,311	(288)
-	-	1,824	22,084	23,908
-	-	9,016	250,695	259,711
<u>\$ -</u>	<u>\$ -</u>	<u>\$ 10,840</u>	<u>\$ 272,779</u>	<u>\$ 283,619</u>

See independent auditor's report.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Combining Statement of Cash Flows

For the Year Ended June 30, 2020

(In Thousands)

	Small System Technical Assistance	Well Head Protection
Cash flows from operating activities		
Financing fee income received	\$ -	\$ -
Cash paid for program administration	-	-
Net cash provided (used) by operating activities	<u>-</u>	<u>-</u>
Cash flows from noncapital financing activities		
Repayments of long-term debt	-	-
Cash paid for interest	-	-
Transfers (out) in	-	(656)
Nonoperating grants received	-	656
Net cash provided by noncapital financing activities	<u>-</u>	<u>-</u>
Cash flows from investing activities		
Interest received on investments	-	-
Interest received on loans	-	-
Principal repayments on loans	-	-
Loan disbursements	-	-
Federal grant funds expended	-	-
Proceeds from maturities of investments	-	-
Net cash provided by investing activities	<u>-</u>	<u>-</u>
Net increase in cash and cash equivalents	-	-
Cash and cash equivalents - beginning of year	<u>-</u>	<u>-</u>
Cash and cash equivalents - end of year	<u>\$ -</u>	<u>\$ -</u>
Reconciliation of changes in net assets to net cash provided by operating activities		
Operating income	\$ -	\$ -
Adjustments to reconcile operating income of changes in net assets in net cash provided (used) by operating activities		
Interest on investments	-	-
Interest on loans	-	-
Bond interest	-	-
Amortization of bond premiums	-	-
Net appreciation of investments	-	-
Federal grants expended	-	-
Changes in operating assets and liabilities		
Accounts receivable - borrowers	-	-
Receivable from other funds	-	-
Accounts payable	-	-
Net cash provided (used) by operating activities	<u>\$ -</u>	<u>\$ -</u>

<u>Capacity Development</u>	<u>State Program Management</u>	<u>Fees and Expenses</u>	<u>Revolving Loan Fund</u>	<u>Total</u>
\$ -	\$ -	\$ 1,489	\$ -	\$ 1,489
-	-	(172)	(20)	(192)
-	-	1,317	(20)	1,297
-	-	-	(2,065)	(2,065)
-	-	-	(702)	(702)
(1,570)	(942)	(450)	3,310	(308)
1,570	942	835	17,434	21,437
-	-	385	17,977	18,362
-	-	105	1,408	1,513
-	-	47	2,642	2,689
-	-	3,493	12,283	15,776
-	-	-	(30,417)	(30,417)
-	-	-	(2,590)	(2,590)
-	-	-	46,006	46,006
-	-	3,645	29,332	32,977
-	-	5,347	47,289	52,636
-	-	5,507	67,765	73,272
\$ -	\$ -	\$ 10,854	\$ 115,054	\$ 125,908
\$ -	\$ -	\$ 1,546	\$ 1,339	\$ 2,885
-	-	(94)	(1,286)	(1,380)
-	-	(49)	(2,633)	(2,682)
-	-	-	694	694
-	-	-	(249)	(249)
-	-	-	(455)	(455)
-	-	-	2,590	2,590
-	-	(42)	-	(42)
-	-	(54)	-	(54)
-	-	10	(20)	(10)
\$ -	\$ -	\$ 1,317	\$ (20)	\$ 1,297

See independent auditor's report.

**Independent Auditor’s Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of Financial
Statements Performed in Accordance With *Government Auditing Standards***

Commissioners of the Arkansas Natural
Resources Commission

Board of Directors
Arkansas Development Finance Authority
Little Rock, Arkansas

We have audited, 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, the combined financial statements of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program (the “Program”), which comprise the combined statement of net position as of June 30, 2020, and the related combined statements of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the basic combined financial statements, and have issued our report thereon dated November 2, 2020, which contained an “emphasis of matter” paragraph regarding a definition of the reporting entity.

Internal Control Over Financial Reporting

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Program's combined financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

Frost, PLLC

Certified Public Accountants

Little Rock, Arkansas
November 2, 2020

**Independent Auditor's Report on Compliance for Each
Major Federal Program and Report on Internal Control
Over Compliance in Accordance With the Uniform Guidance**

Commissioners of the Arkansas Natural
Resources Commission

Board of Directors
Arkansas Development Finance Authority
Little Rock, Arkansas

Report on Compliance for Each Major Federal Program

We have audited the State of Arkansas Safe Drinking Water Revolving Loan Fund Program's (the "Program") compliance with the types of compliance requirements described in the U.S. Office of Management and Budget *Compliance Supplement* that could have a direct and material effect on each of the Program's major federal programs for the year ended June 30, 2020. The Program's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Program's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles and Audit Requirements for Federal Awards* ("Uniform Guidance"). Those standards and Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Program's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Program's compliance.

Opinion on Each Major Federal Program

In our opinion, the Program complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2020.

Report on Internal Control Over Compliance

Management of the Program is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Program's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Program's internal control over compliance.

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

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

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Frost, PLLC

Certified Public Accountants

Little Rock, Arkansas
November 2, 2020

STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2020

Section I – Summary of Auditor’s Results

Combined Financial Statements

Type of auditor’s report issued: Unmodified

Internal control over financial reporting:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None Reported

Noncompliance material to combined financial statements noted? Yes No

Federal Awards

Internal control over major programs:

- Material weakness(es) identified? Yes No
- Significant deficiency(ies) identified? Yes None Reported

Type of auditor’s report issued on compliance for major federal programs. Unmodified

Are any audit findings disclosed that are required to be reported in accordance with 2 CFR 200.516(a)? Yes No

Identification of major federal programs:

CFDA Number(s) and Name of Federal Program or Cluster

Capitalization Grants for Drinking Water State Revolving Funds 66.468

Dollar threshold used to distinguish between type A and type B programs: \$ 750,000

Auditee qualified as a low-risk auditee? Yes No

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

Summary Schedule of Prior Audit Findings

For the Year Ended June 30, 2020

<u>Reference Number</u>	<u>Summary of Finding</u>	<u>Status</u>
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No matters are reportable.

STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM

Schedule of Expenditures of Federal Awards

For the Year Ended June 30, 2020

(In Thousands)

<u>Federal Grantor/Pass-Through Grantor Program or Cluster Title</u>	<u>Federal CFDA Number</u>	<u>Provided to Subrecipients</u>	<u>Total Federal Expenditures</u>
U.S. Environmental Protection Agency/Capitalization Grants for Drinking Water State Revolving Funds (Drinking Water State Revolving Fund Cluster)	66.468	\$ 17,434	\$ 21,311

The accompanying notes are an integral part of the schedule of expenditures of federal awards.

**STATE OF ARKANSAS SAFE DRINKING WATER
REVOLVING LOAN FUND PROGRAM**

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Notes to Schedule of Expenditures of Federal Awards

For the Year Ended June 30, 2020

1. The accompanying schedule of expenditures of federal awards (“SEFA”) includes the federal award activity of the State of Arkansas Safe Drinking Water Revolving Loan Fund Program (the “Program”) under programs of the federal government for the year ended June 30, 2020. The information in the SEFA is presented in accordance with the requirements of Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (“Uniform Guidance”). Because the SEFA presents only a selected portion of the operations of the Program, it is not intended to and does not present the net position, changes in net position or cash flows of the Program.
2. Expenditures reported on the SEFA are reported on the accrual basis of accounting. Such expenditures are recognized following, as applicable, the cost principles in U.S. Office of Management and Budget A-110 or contained in the Uniform Guidance, wherein certain types of expenditures are not allowable or are limited as to reimbursement. The Program has elected not to use the 10% de minimis indirect cost rate allowed under the Uniform Guidance.
3. Expenditures reflected in CFDA 66.468, Capitalization Grants for Drinking Water State Revolving Funds, include loans to counties, municipalities and other tax-exempt water system entities for construction of new water systems, expansion or repair of existing water systems and/or consolidation of new or existing water systems. The funding source for these loans includes federal grant funds, state match funds, bond funds and revolving Program funds. The funds are disbursed to the subrecipients after expenses have been incurred as forgiveness of principal and repayable loans. The Program’s outstanding loan receivable balance from subrecipients from all funding sources was \$171.6 million for the year ended June 30, 2020. Total federal loan disbursements totaled \$17.4 million during fiscal year 2020. Total loans forgiven totaled \$2.6 million during fiscal year 2020. For the year ended June 30, 2020, the Program received \$3.9 million in federal funds for administrative costs, which were disbursed to the administration agencies.