SOUTH DAKOTA BOARD OF WATER
AND NATURAL RESOURCES
CLEAN WATER STATE REVOLVING FUND

AUDIT REPORT

Fiscal Year Ended June 30, 2014

State of South Dakota
Department of Legislative Audit
427 South Chapelle
500 East Capitol
Pierre, SD 57501-5070
SOUTH DAKOTA BOARD OF WATER
AND NATURAL RESOURCES
CLEAN WATER STATE REVOLVING FUND
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BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Honorable Dennis Daugaard
Governor of South Dakota

and

South Dakota Board of Water and Natural Resources

We have audited, in accordance with the 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 financial statements of the Clean Water State Revolving Fund, which comprise the statement of net position as of June 30, 2014, and the related statements of revenues, expenses and changes in fund net position, and cash flows for the year ended, and the related notes to the financial statements, which collectively comprise the Clean Water State Revolving Fund’s basic financial statements, and have issued our report thereon dated December 9, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the South Dakota Board of Water and Natural Resources' internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the South Dakota Board of Water and Natural Resources' internal control. Accordingly, we do not express an opinion on the effectiveness of the South Dakota Board of Water and Natural Resources' 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 combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's 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 was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control 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 South Dakota Board of Water and Natural Resources’ 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. As required by South Dakota Codified Law 4-11-11, this report is a matter of public record and its distribution is not limited.

[Signature]

Martin L. Guindon, CPA
Auditor General

December 9, 2014
INDEPENDENT AUDITOR’S REPORT

The Honorable Dennis Daugaard
Governor of South Dakota

and

South Dakota Board of Water and Natural Resources

Report on the Financial Statements

We have audited the accompanying financial statements of the Clean Water State Revolving Fund, a fund of the Board of Water and Natural Resources, a blended component unit of the State of South Dakota, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Clean Water State Revolving Fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor
considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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 Clean Water State Revolving Fund as of June 30, 2014, and the changes in its financial position and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Adoption of New Accounting Standard

As described in Note 1.K. to the financial statements, the Board of Water and Natural Resources adopted the provisions of GASB Statement No. 65, Items Previously Reported as Assets and Liabilities. The Clean Water State Revolving Fund has restated beginning net position to account for bond issuance costs in accordance with this statement. Our opinion is not modified with respect to this matter.

Emphasis of Matter

As described in Note 1.A, the financial statements present only the financial position and changes in financial position and cash flows of the Clean Water State Revolving Fund. They do not purport to, and do not, present fairly the financial position of the Board of Water and Natural Resources as of June 30, 2014, and the changes in its financial position and its cash flows, where applicable, for the year 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 on pages 6-9 be presented to supplement the basic financial statements. Such information, although not a 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.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated December 9, 2014 on our consideration of the South Dakota Board of Water and Natural Resources' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 South Dakota Board of Water and Natural Resources' internal control over financial reporting and compliance.

Martin L. Guindon, CPA
Auditor General

December 9, 2014
This section of the South Dakota Department of Environment and Natural Resources Clean Water State Revolving Fund's (Fund) financial report presents a narrative overview and analysis of the financial activities of the Fund for the fiscal year ended June 30, 2014. This analysis has been prepared by management of the Department, and is intended to be read in conjunction with the Fund's financial statements and related footnotes which follow this section.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the Fund's basic financial statements. The Fund's basic financial statements include: 1) Statement of Net Position, 2) Statement of Revenues, Expenses and Changes in Fund Net Position, 3) Statement of Cash Flows, and 4) Notes to the Financial Statements.

The Statement of Net Position presents information on all of the Fund's assets and liabilities, with the difference between the two reported as net position. The Statement of Revenues, Expenses and Changes in Fund Net Position presents information showing how the Fund's net position changed during the most recent fiscal year.

The Statement of Cash Flows presents the Fund's flows of cash by defined categories. The primary purpose of the Statement of Cash Flows is to provide information about the Fund's cash receipts and payments during the year.

The Notes to the Financial Statements are an integral part of the financial statements and provide additional information that is essential to a full understanding of the data provided in the financial statements.

ANALYSIS OF BALANCES AND TRANSACTIONS OF THE CLEAN WATER STATE REVOLVING FUND

Changes in Net Position

For the fiscal year ended June 30, 2014, net position of the Fund increased by 7.6% - primarily due to total revenues for the fund amounting to $15,714,047 more than total expenses for the Fund. The main reason the total revenue was higher was due to federal capitalization grants under nonoperating revenue being $12.5 million higher in FY14 than in FY13. Operating revenue increased by over 14%, while operating expenses went down by more than 9%. GASB 65 required that the deferred amounts for refunding be broken out separately from bonds payable. This amount is found after the total assets in the table below.
SOUTH DAKOTA BOARD OF WATER AND NATURAL RESOURCES  
CLEAN WATER STATE REVOLVING FUND  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
(Continued)  

<table>
<thead>
<tr>
<th>NET POSITION</th>
<th>2014</th>
<th>2013</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Assets</td>
<td>$39,895,763</td>
<td>$75,123,910</td>
<td>-46.9%</td>
</tr>
<tr>
<td>Noncurrent Assets</td>
<td>312,902,430</td>
<td>270,910,811</td>
<td>15.5%</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>352,798,193</td>
<td>346,034,721</td>
<td>2.0%</td>
</tr>
<tr>
<td>Deferred Amount of Refunding</td>
<td>3,964,749</td>
<td></td>
<td>N/A</td>
</tr>
<tr>
<td><strong>Total Deferred Outflow of Resources</strong></td>
<td>3,964,749</td>
<td>0</td>
<td>N/A</td>
</tr>
<tr>
<td>Current Liabilities</td>
<td>10,904,103</td>
<td>10,911,663</td>
<td>-0.1%</td>
</tr>
<tr>
<td>Noncurrent Liabilities</td>
<td>136,348,558</td>
<td>140,421,691</td>
<td>-2.9%</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td>147,252,661</td>
<td>151,333,354</td>
<td>-2.7%</td>
</tr>
<tr>
<td>Net Position:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Restricted</td>
<td>98,749</td>
<td>98,749</td>
<td>0.0%</td>
</tr>
<tr>
<td>Unrestricted</td>
<td>209,411,531</td>
<td>194,602,618</td>
<td>7.6%</td>
</tr>
<tr>
<td><strong>Total Net Position</strong></td>
<td>$209,510,280</td>
<td>$194,701,367</td>
<td>7.6%</td>
</tr>
<tr>
<td></td>
<td>2014</td>
<td>2013</td>
<td>% Change</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>--------</td>
<td>--------</td>
<td>----------</td>
</tr>
<tr>
<td>Loan Int. Income</td>
<td>$4,687,315</td>
<td>$4,039,336</td>
<td>16.0%</td>
</tr>
<tr>
<td>Other Income</td>
<td>1,331,579</td>
<td>1,237,680</td>
<td>7.6%</td>
</tr>
<tr>
<td>Total Operating Revenue</td>
<td>6,018,894</td>
<td>5,277,016</td>
<td>14.1%</td>
</tr>
<tr>
<td>Administrative Expenses</td>
<td>1,441,428</td>
<td>2,760,295</td>
<td>-47.8%</td>
</tr>
<tr>
<td>Grant Expenses</td>
<td>2,468,382</td>
<td>1,877,115</td>
<td>31.5%</td>
</tr>
<tr>
<td>Interest Expense</td>
<td>5,186,694</td>
<td>5,404,346</td>
<td>-4.0%</td>
</tr>
<tr>
<td>Arbitrage</td>
<td>766,316</td>
<td>775,604</td>
<td>-1.2%</td>
</tr>
<tr>
<td>Bond Issuance Expense**</td>
<td></td>
<td>51,856</td>
<td>-100.0%</td>
</tr>
<tr>
<td>Total Operating Expenses**</td>
<td>9,862,820</td>
<td>10,869,216</td>
<td>-9.3%</td>
</tr>
<tr>
<td>Operating Loss</td>
<td>(3,843,926)</td>
<td>(5,592,200)</td>
<td>31.3%</td>
</tr>
<tr>
<td>Federal Cap Grants</td>
<td>15,144,209</td>
<td>2,616,290</td>
<td>478.8%</td>
</tr>
<tr>
<td>Other Income</td>
<td>425,375</td>
<td>462,113</td>
<td>-8.0%</td>
</tr>
<tr>
<td>Investment Income</td>
<td>4,005,146</td>
<td>3,429,428</td>
<td>16.8%</td>
</tr>
<tr>
<td>Investment Expense</td>
<td>(16,757)</td>
<td>(27,858)</td>
<td>-39.8%</td>
</tr>
<tr>
<td>Non Operating Rev (Exp)</td>
<td>19,557,973</td>
<td>6,479,973</td>
<td>201.8%</td>
</tr>
<tr>
<td>Transfers</td>
<td>(31,963)</td>
<td>(30,031)</td>
<td>6.4%</td>
</tr>
<tr>
<td>Change in Net Position</td>
<td>15,682,084</td>
<td>857,740</td>
<td>1,728.3%</td>
</tr>
<tr>
<td>Beginning Net Position *</td>
<td>193,828,196</td>
<td>193,843,627</td>
<td>0.0%</td>
</tr>
<tr>
<td>Total Net Position</td>
<td>$209,510,280</td>
<td>$194,701,367</td>
<td>7.6%</td>
</tr>
</tbody>
</table>

*2014 was restated in accordance with GASB Statement 65
**As of FY14, GASB 65 no longer allows the amortizing of bond issuance costs.
ECONOMIC OUTLOOK

The South Dakota economy has been in a recovery phase for nearly four years as increases in employment, income, and overall spending have been rebounding since early 2010. However, the pace of the recovery has been mixed, with employment growth being sluggish but income growth being stronger. Strength in the agriculture sector has supported income growth directly and indirectly as record farm income in recent years helped boost South Dakota’s economy. State tax revenue for fiscal year 2014 increased 2.7% over last year.

The state is challenged demographically with a large number of small rural communities and only two cities with populations over 50,000 people. The Clean Water State Revolving Fund assists the state in meeting these challenges and infrastructure needs. In state fiscal year 2014, the State of South Dakota obligated $18.325 million to 20 projects.
SOUTH DAKOTA BOARD OF WATER
AND NATURAL RESOURCES
CLEAN WATER STATE REVOLVING FUND
STATEMENT OF NET POSITION
June 30, 2014

Assets

Current Assets:
Cash and Cash Equivalents $11,033,053.58
Restricted Cash and Cash Equivalents 2,978.48
Total Cash and Cash Equivalents $11,036,032.06

Investments 2,800,752.71
Due From Federal Government 62,997.65
Due From Other Governments 394,804.23
Accrued Interest Receivable 3,092,126.05
Loans Receivable 22,509,049.95
Total Current Assets $39,895,762.65

Noncurrent Assets:
Investments 84,288,253.83
Restricted Investments 95,770.84
Loans Receivable 228,518,405.24
Total Noncurrent Assets $312,902,429.91

Total Assets $352,798,192.56

Deferred Outflow of Resources
Deferred Charge on Refunding $3,964,748.51
Total Deferred Outflows of Resources $3,964,748.51

Liabilities

Current Liabilities:
Accounts Payable 210,444.42
Accrued Liabilities 20,816.67
Compensated Absences Payable 38,449.26
Accrued Interest Payable 2,225,711.45
Arbitrage Payable 280,317.41
Bonds Payable - net of unamortized premium 8,128,363.96
Total Current Liabilities $10,904,103.17

Noncurrent Liabilities:
Compensated Absences Payable 34,316.18
Arbitrage Payable 275,283.99
Bonds Payable - net of unamortized premium 136,038,957.28
Total Noncurrent Liabilities $136,348,557.45

Total Liabilities $147,252,660.62

Net Position
Restricted For Debt Service 98,749.32
Unrestricted 209,411,531.13

Total Net Position $209,510,280.45

The notes to the financial statements are an integral part of this statement.
SOUTH DAKOTA BOARD OF WATER
AND NATURAL RESOURCES
CLEAN WATER STATE REVOLVING FUND
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION
For the Fiscal Year Ended June 30, 2014

Operating Revenues:
Loan Interest Income $ 4,887,315.11
Other Income 1,331,579.50
Total Operating Revenue 6,018,894.61

Operating Expenses:
Administrative Expenses
Personal Services 229,957.60
Employee Benefits 66,100.90
Travel 12,908.01
Contractual 363,108.91
Supplies 1,382.06
Grants 767,555.75
Other 415.00
Total Administrative Expenses 1,441,428.23
Grant Expense 2,468,382.00
Interest Expense 5,186,693.61
Arbitrage Rebate 766,316.53
Total Operating Expenses 9,862,820.37

Operating Income (Loss) (3,843,925.76)

Nonoperating Revenues (Expenses):
Federal Capitalization Grants 15,144,209.31
Other Income 425,374.56
Investment Income 4,005,146.07
Investment Expense (16,756.72)
Total Nonoperating Revenues (Expenses) 19,557,973.22

Income (Loss) Before Transfers 15,714,047.46

Transfers:
Transfers Out (31,962.70)

Change in Net Position 15,682,084.76

Net Position at Beginning of Year, restated 193,828,195.69

Net Position at End of Year $ 209,510,280.45

The notes to the financial statements are an integral part of this statement.
# SOUTH DAKOTA BOARD OF WATER AND NATURAL RESOURCES
## CLEAN WATER STATE REVOLVING FUND
### STATEMENT OF CASH FLOWS
#### For the Fiscal Year Ended June 30, 2014

### Cash Flows from Operating Activities:
- Receipts for Loan Repayments $18,346,753.92
- Receipts for Interest Income on Loans 4,079,476.75
- Receipts for Surcharge Interest on Loans 1,206,946.05
- Payments to Loan Recipients (52,418,444.00)
- Arbitrage Payment (1,074,396.48)
- Payments for Employee Services (294,071.64)
- Payments for Contractual Services (405,007.60)
- Payment for Grants (811,045.05)
- Payment for Principal Forgiveness (2,468,382.00)
- Other Payments (13,016.92)

Net Cash Provided (Used) by Operating Activities (33,851,186.95)

### Cash Flows from Noncapital Financing Activities:
- Transfers Out (31,962.70)
- Principal Payments on Bonds (7,415,000.00)
- Interest Payments on Bonds (5,427,342.49)
- Receipts for Administering Program 15,178,181.00
- Other Income 425,374.56

Net Cash Provided (Used) by Noncapital Financing Activities 2,729,250.37

### Cash Flows from Investing Activities:
- Interest on Investments 3,860,201.40
- Proceeds from Sale of Investment Securities 19,084,436.72
- Purchase of Investment Securities (35,937,717.36)

Net Cash Provided (Used) by Investing Activities (12,993,079.26)

Net Increase (Decrease) in Cash and Cash Equivalents (44,115,015.84)

Cash and Cash Equivalents at Beginning of Year 55,151,047.90

Cash and Cash Equivalents at End of Year $ 11,036,032.06

### Reconciliation of Operating Income to Net
- Cash Provided (Used) by Operating Activities Operating Income (Loss) $ (3,843,925.76)

### Adjustments to Reconcile Net Income to Net Cash Provided (Used) by Operating Activities:
- Interest Expense 5,186,693.61
- Assets: (Increase)/Decrease
  - Loans Receivable (34,071,690.08)
  - Accrued Interest Receivable on Loans (607,838.36)
  - Due from Other Governments (124,633.45)
- Liabilities: Increase/(Decrease)
  - Accounts Payable (83,699.84)
  - Accrued Employee Benefits (2,396.07)
  - Accrued Liabilities 4,382.93
  - Arbitrage (308,079.93)

Total Adjustments (30,007,261.19)

Net Cash Provided by Operations $ (33,851,186.95)

The notes to the financial statements are an integral part of this statement.
1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Authorizing Legislation

The 1988 South Dakota Legislature authorized the State Water Pollution Control Revolving Loan Fund Program, also known as the Clean Water State Revolving Fund (CWSRF) Loan Program. Additionally, the legislature appropriated $1,200,000 and directed the South Dakota Conservancy District (SDCD) to administer the program. The SDCD was created by the Legislature under Chapter 46A-2 of the South Dakota Codified Law as a body politic and corporate for the purpose of constructing water resource facilities for the conservation, storage, distribution and utilization of water for municipal purposes within the State of South Dakota. The SDCD bonds do not constitute a debt of the State of South Dakota, or a pledge of the faith and credit of the State. Because the State of South Dakota is able to impose its will over the SDCD and the governing body is substantively the same as the governing body of the primary government, it is considered a blended component unit and, as such, the accompanying financial statements are included in the Comprehensive Annual Financial Report of the State of South Dakota. The Department of Environment and Natural Resources performs all of the functions of the South Dakota Conservancy District, except for quasi-legislative, quasi-judicial, advisory, and special budgetary functions, which are performed by the Board of Water and Natural Resources acting in its capacity as the Conservancy District. The CWSRF is a low interest loan program to finance the construction of wastewater facilities, storm sewers and non-point source pollution control projects. The program was created by the 1987 Clean Water Act amendments. Funds are provided to the states in the form of capitalization grants awarded annually through the United States Environmental Protection Agency. The federal capitalization grants are matched by state funds at a ratio of 5:1.

B. Fund Accounting

The CWSRF is accounted for as an enterprise fund. An enterprise fund is a proprietary fund type used to report an activity for which a fee is charged to external users for goods or services.

C. Basis of Accounting

The CWSRF follows the accrual basis of accounting. This method of accounting recognizes the financial effect of transactions, events, and interfund activities when they occur, regardless of the timing of related cash flows.

D. Cash and Cash Equivalents

For purposes of the accompanying statement of net position and statement of cash flows all highly liquid investments with original maturities of 90 days or less are considered to be cash equivalents.
E. Investments

Investments are reported at fair value. Unrealized gains and losses due to fluctuations in market value are included in investment income.

F. Premiums and Deferred Amounts on Refunding

Premiums and the deferred amount of refunding on bonds are amortized using the straight line method over the life of the bonds to which they relate.

G. Reserves

The bond indentures provide that certain reserve accounts be established. The reserves as of June 30, 2014, consist of the following Investment Agreement and are reported as restricted net position in the financial statements:

- 6.22% MBIA Inc. due August 1, 2017 totaling $95,770.84

In addition, $2,978.48 is invested in a Money Market Fund described in note 2 below.

H. Restricted Resources

When both restricted and unrestricted resources are available for use, it is the CWSRF’s policy to use restricted resources first, and then unrestricted resources as they are needed.

I. Revenue and Expense Recognition

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering items in connection with an enterprise fund’s principal ongoing operations. The CWSRF records all revenues derived from interest on loans as operating revenues since these revenues are generated from the CWSRF’s daily operations needed to carry out its purpose. Operating expenses include grants and subsidies, and contractual service expenses related to the administration of the CWSRF program.

J. Federal Capitalization Grant

Federal capitalization grants reported as nonoperating income in the statement of revenues, expenses, and changes in fund net position is a federally funded loan program. Information about the program is as follows:

| CFDA Number: | 66.458 |
| Federal Agency: | Environmental Protection Agency |
| Program: | Clean Water State Revolving Fund |
| State Agency: | Environment & Natural Resources |
| Outstanding Loans: | $251,027,455 |
| Current Year Administrative Expense: | $419,737 |
| Loan Disbursement: | $54,886,826 |
K. GASB 65

GASB 65 changed the way bond issuance costs are accounted for. They are no longer allowed to be amortized, but must be fully expensed when the bonds are issued. To adjust for bond issuance costs previously being amortized, the Beginning Net Position was restated by $873,171.13. Also, GASB 65 required that deferred amount of refunding be reported as a deferred outflow of resources on the Statement of Net Position.

2. CASH AND INVESTMENTS

Cash and Cash Equivalents consisted of a Goldman Sachs Financial Square Treasury Obligation Fund (money market fund) and the South Dakota Cash Flow Fund. The Goldman Sachs Fund was rated "AAAm" by Standard and Poor's Rating Group. The fund paid less than .01% for the period 7/01/2013- 6/30/2014. The South Dakota Conservancy District Investment Policy adopted pursuant to the Master Trust Indenture authorizes the investment of up to 20 percent of funds in the South Dakota Cash Flow portfolio which is an unrated fund. The fund paid 0.99% for state fiscal year 2014.

Management of the State’s internal investment pool is the statutory responsibility of the South Dakota Investment Council (SDIC). The investment policy and required risk disclosures for the State’s internal investment pool are presented in the audit report of the South Dakota Investment Council, which can be obtained by contacting the Department of Legislative Audit, 427 South Chapelle, c/o 500 East Capitol, Pierre, South Dakota 57501.

Custodial Credit Risk: Custodial credit risk is the risk that in the event of a bank failure, the Clean Water State Revolving Fund’s investments may not be returned. At June 30, 2014, $78,349,144 of guaranteed investment contracts were uninsured and unregistered, with the securities held by its trust department, but not in the CWSRF’s name and, as a result, were exposed to custodial credit risk. Also, investments were made in US Treasury Bonds with a market value of $5,852,622 and in Federal Agency Bonds with a market value of $2,971,928 were exposed to custodial credit risk.

Interest Rate Risk: Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The maturities of the investments are listed below.

<table>
<thead>
<tr>
<th>Investment</th>
<th>Maturities</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Guaranteed Investment Contract</td>
<td>8/01/2017</td>
<td>$1,290,425</td>
</tr>
<tr>
<td>Guaranteed Investment Contract</td>
<td>8/01/2025</td>
<td>16,510,415</td>
</tr>
<tr>
<td>Guaranteed Investment Contract</td>
<td>8/01/2026</td>
<td>60,548,304</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$78,349,144</td>
</tr>
<tr>
<td>US Treasury Bonds</td>
<td>11/30/2014</td>
<td>$433,647</td>
</tr>
<tr>
<td>US Treasury Bonds</td>
<td>2/28/2015</td>
<td>340,065</td>
</tr>
<tr>
<td>US Treasury Bonds</td>
<td>5/31/2015</td>
<td>2,036,260</td>
</tr>
<tr>
<td>US Treasury Bonds</td>
<td>11/30/2015</td>
<td>2,032,340</td>
</tr>
<tr>
<td>US Treasury Bonds</td>
<td>8/31/2016</td>
<td>1,010,310</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$5,852,622</td>
</tr>
<tr>
<td>Federal Agency Bonds</td>
<td>3/30/2016</td>
<td>$305,528</td>
</tr>
<tr>
<td>Federal Agency Bonds</td>
<td>4/27/2017</td>
<td>352,184</td>
</tr>
<tr>
<td>Federal Agency Bonds</td>
<td>8/28/2017</td>
<td>622,381</td>
</tr>
<tr>
<td>Federal Agency Bonds</td>
<td>10/26/2017</td>
<td>496,835</td>
</tr>
<tr>
<td>Federal Agency Bonds</td>
<td>12/20/2017</td>
<td>504,905</td>
</tr>
<tr>
<td>Federal Agency Bonds</td>
<td>3/07/2018</td>
<td>690,095</td>
</tr>
<tr>
<td></td>
<td></td>
<td>$2,971,928</td>
</tr>
</tbody>
</table>
Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the CWSRF. The South Dakota State Revolving Fund Master Trust Indenture requires any investment agreement to be with a guarantor whose long-term rating category is no lower than the two highest long-term rating categories. The investment is rated by Moody’s Investors Service. The ratings for Guaranteed Investment Contracts are as follows:

<table>
<thead>
<tr>
<th>Moody’s Rating</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ba1*</td>
<td>$1,290,425</td>
</tr>
<tr>
<td>Baa1*</td>
<td>77,058,719</td>
</tr>
<tr>
<td>Total</td>
<td>$78,349,144</td>
</tr>
</tbody>
</table>

* These guarantor's ratings are below the acceptable rating category (i.e., below Moody’s Aa3). The Guaranteed Investment Contract investments have been fully collateralized with government securities in accordance with the provisions of Guaranteed Investment Contracts. These fully collateralized investments have a fair value that equates to contract value.

Excluding investments explicitly guaranteed by the U.S. Government which are not considered to have credit risk, the CWSRF held Federal Agency Bonds with a fair value of $2,971,928 which were rated Aaa by Moody’s Investor Services.

3. LOANS RECEIVABLE

Loans receivable consist of loans made to local governments through a loan agreement. In order for a local government to receive a loan, evidence must be shown that the principal and interest of the loan will be repaid. Therefore, each local government must show the ability to impose utility rates, levy special assessments or collect sales taxes that will generate enough revenue to equal at least 110% of the annual principal and interest on the loan. Loans made from the CWSRF may be made at or below market interest rates and shall be fully amortized within twenty years of the date which is not more than one year following completion of the project financed. Interest rates are reduced for those loans shorter than twenty years. Of the $251,027,455 loan receivable balance, $17,579,104 is a long term receivable balance and $407,320 is a short term receivable balance for the Ellisworth Development Authority which is a component unit of the State of South Dakota.
4. **LONG-TERM DEBT**

**Revenue Bonds**

The bond issues outstanding as of June 30, 2014 are as follows:

<table>
<thead>
<tr>
<th>Issue</th>
<th>Interest Rate</th>
<th>Maturity Through</th>
<th>Principal Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Series 1996 A</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Term Bonds</td>
<td>5.625%</td>
<td>2017</td>
<td>$ 100,000</td>
</tr>
<tr>
<td>Series 2010AB</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Build America Bonds (BABs)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Match</td>
<td>4.084% - 5.646%</td>
<td>2031</td>
<td>2,430,000</td>
</tr>
<tr>
<td>Leveraged</td>
<td>4.084% - 5.646%</td>
<td>2031</td>
<td>23,600,000</td>
</tr>
<tr>
<td>Tax Exempt Bonds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Match</td>
<td>4.084% - 5.646%</td>
<td>2030</td>
<td>2,170,000</td>
</tr>
<tr>
<td>Leveraged</td>
<td>4.084% - 5.646%</td>
<td>2030</td>
<td>21,600,000</td>
</tr>
<tr>
<td>Series 2012AB</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Taxable Revenue Bonds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Match</td>
<td>0.250% - 3.183%</td>
<td>2027</td>
<td>2,305,000</td>
</tr>
<tr>
<td>Leveraged</td>
<td>0.250% - 3.183%</td>
<td>2027</td>
<td>33,435,000</td>
</tr>
<tr>
<td>Revenue Bonds</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Match</td>
<td>2.000% - 5.000%</td>
<td>2030</td>
<td>3,240,000</td>
</tr>
<tr>
<td>Leveraged</td>
<td>2.000% - 5.000%</td>
<td>2033</td>
<td>45,340,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td><strong>134,220,000</strong></td>
</tr>
</tbody>
</table>

Add: Unamortized Bond Premium

**Total Net of Amortization**

$ 144,167,321

Future bond payments and future interest payments remaining as of June 30, 2014 are as follows:

<table>
<thead>
<tr>
<th>Year Ended June 30,</th>
<th>Principal</th>
<th>Interest</th>
<th>Total Principal and Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
<td>$ 7,580,000</td>
<td>$ 5,240,680</td>
<td>$ 12,820,680</td>
</tr>
<tr>
<td>2016</td>
<td>7,460,000</td>
<td>5,024,255</td>
<td>12,484,255</td>
</tr>
<tr>
<td>2017</td>
<td>7,500,000</td>
<td>4,799,669</td>
<td>12,299,669</td>
</tr>
<tr>
<td>2018</td>
<td>7,710,000</td>
<td>4,556,284</td>
<td>12,266,284</td>
</tr>
<tr>
<td>2019</td>
<td>7,780,000</td>
<td>4,300,777</td>
<td>12,080,777</td>
</tr>
<tr>
<td>2020-2024</td>
<td>39,425,000</td>
<td>17,567,110</td>
<td>56,992,110</td>
</tr>
<tr>
<td>2025-2029</td>
<td>38,270,000</td>
<td>8,809,381</td>
<td>47,079,381</td>
</tr>
<tr>
<td>2030-2033</td>
<td>18,495,000</td>
<td>1,556,174</td>
<td>20,051,174</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td>$ 134,220,000</td>
<td>$ 51,854,330</td>
<td>$ 186,074,330</td>
</tr>
</tbody>
</table>
Changes in long-term liabilities

<table>
<thead>
<tr>
<th></th>
<th>Beginning Balance</th>
<th>Additions</th>
<th>Reductions</th>
<th>Ending Balance</th>
<th>Due Within One Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue Bonds</td>
<td>$141,635,000</td>
<td>$0</td>
<td>($7,415,000)</td>
<td>$134,220,000</td>
<td>$7,580,000</td>
</tr>
<tr>
<td>Add: Bond Premium</td>
<td>10,495,685</td>
<td></td>
<td>(548,364)</td>
<td>9,947,321</td>
<td>548,364</td>
</tr>
<tr>
<td>Total</td>
<td>152,130,685</td>
<td>0</td>
<td>(7,963,364)</td>
<td>144,167,321</td>
<td>8,128,364</td>
</tr>
<tr>
<td>Compensated Absences</td>
<td>75,162</td>
<td>22,267</td>
<td>(24,664)</td>
<td>72,765</td>
<td>38,449</td>
</tr>
<tr>
<td>Long-Term Liabilities</td>
<td>$152,205,847</td>
<td>$22,267</td>
<td>($7,988,028)</td>
<td>$144,240,086</td>
<td>$8,166,813</td>
</tr>
</tbody>
</table>

5. COMMITMENTS

As of June 30, 2014, the CWSRF had loan commitments with political subdivisions worth $56,269,735.

6. RETIREMENT PLAN

The Department of Environment and Natural Resources participates in the South Dakota Retirement System (SDRS) a cost-sharing, multiple employer defined benefit pension plan established to provide retirement, disability, and survivor benefits for employees of the State and its political subdivisions. Authority for establishing, administering and amending plan provisions is found in SDCL 3-12. The SDRS issues a publicly available financial report that includes financial statements, footnote disclosures, and required supplementary information. That report may be obtained by writing to the SDRS, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731.

Employees are required by state statute to contribute 6 percent of their salary to the plan. State statute also requires the employer to contribute an amount equal to the employee's contribution. The right to receive retirement benefits vests after three years of credited service. The CWSRF contributions to the SDRS for the fiscal years ended June 30, 2014, 2013, and 2012, were $15,460.85, $13,751.34, and $13,580.48, respectively, equal to the required contributions each year.

7. ANNUAL AND SICK LEAVE ACCRUAL

All employees earn annual leave. Upon termination, employees are eligible to receive compensation for their accrued annual leave balances. At June 30, 2014, a liability existed for accumulated annual leave calculated at the employee's June 30, 2014 pay rate in the amount of $30,876.94. Employees who have been continuously employed by the State of South Dakota for at least seven years prior to the date of their retirement, voluntary resignation or death will receive payment for one-fourth of their accumulated sick leave balance. This payment is not to exceed the sum of twelve weeks of employee's annual compensation. At June 30, 2014, a liability existed for accumulated sick leave, calculated at each employee's June 30, 2014 pay rate in the amount of $41,888.50. The total leave liability of $72,765.44 at June 30, 2014 is shown as a liability on the balance sheet.
8. RISK MANAGEMENT

The Department of Environment and Natural Resources is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The Department is uninsured for property loss. The Department participates in the various programs administered by the State of South Dakota. These risk management programs are funded through assessments charged to participating entities. The risk management programs include: 1) coverage for risks associated with automobile liability and general tort liability (including public officials' errors and omissions liability, medical malpractice liability, law enforcement liability, and products liability) through the State’s Public Entity Pool for Liability Fund, 2) coverage of employee medical claims through the State’s health insurance program, 3) coverage for unemployment benefits through the State’s Unemployment Insurance Fund, and, 4) coverage for workers’ compensation benefits through the State’s Workers’ Compensation Fund. Financial information relative to the self-insurance funds administered by the State is presented in the State of South Dakota Comprehensive Annual Financial Report.

9. SUBSEQUENT EVENTS

In October 2014, the South Dakota Conservancy District issued its State Revolving Fund Program Bonds, Series 2014 consisting of $9,060,000 principal amount of Taxable Revenue Bonds, Series 2014A and $50,775,000 principal amount Revenue Bonds, Series 2014B. The following is a summary of the estimated sources and uses of Series 2014 Bonds:

<table>
<thead>
<tr>
<th>Sources:</th>
<th>Series 2014A (Taxable)</th>
<th>Series 2014B (Tax-Exempt)</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bond Proceeds (Par)</td>
<td>$ 9,060,000</td>
<td>$ 50,755,000</td>
<td>$ 59,815,000</td>
</tr>
<tr>
<td>Premium</td>
<td>9,601,865</td>
<td>9,601,865</td>
<td>9,601,865</td>
</tr>
<tr>
<td>Total Sources of Funds</td>
<td>$ 9,060,000</td>
<td>$ 60,356,865</td>
<td>$ 69,416,865</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Uses:</th>
<th>Series 2014A (Taxable)</th>
<th>Series 2014B (Tax-Exempt)</th>
<th>Totals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposit to Clean Water State Match Loan Fund</td>
<td>$ 4,000,000</td>
<td>$</td>
<td>$ 4,000,000</td>
</tr>
<tr>
<td>Deposit to Clean Water Leveraged Loan Fund</td>
<td>53,000,000</td>
<td>53,000,000</td>
<td>53,000,000</td>
</tr>
<tr>
<td>Deposit to Drinking Water State Match Loan Fund</td>
<td>5,000,000</td>
<td>7,000,000</td>
<td>7,000,000</td>
</tr>
<tr>
<td>Deposit to Drinking Water Leveraged Loan Fund</td>
<td>356,865</td>
<td>416,865</td>
<td>416,865</td>
</tr>
<tr>
<td>Cost of Issuance</td>
<td>60,000</td>
<td>356,865</td>
<td>416,865</td>
</tr>
<tr>
<td>Total Uses of Funds</td>
<td>$ 9,060,000</td>
<td>$ 60,356,865</td>
<td>$ 69,416,865</td>
</tr>
</tbody>
</table>
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