

**STATE OF CONNECTICUT CLEAN WATER FUND -  
DRINKING WATER FEDERAL REVOLVING  
LOAN ACCOUNT (STATE REVOLVING FUND)**

**AUDIT REPORTS AND SCHEDULES IN  
ACCORDANCE WITH OMB CIRCULAR A-133**

**June 30, 2012 and 2011**

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**STATE OF CONNECTICUT CLEAN WATER FUND -  
DRINKING WATER FEDERAL REVOLVING  
LOAN ACCOUNT (STATE REVOLVING FUND)  
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# SEWARD AND MONDE

CERTIFIED PUBLIC ACCOUNTANTS  
296 STATE STREET  
NORTH HAVEN, CONNECTICUT 06473-2165  
(203) 248-9341  
FAX (203) 248-5813

## INDEPENDENT AUDITORS' REPORT

Ms. Denise L. Nappier, Treasurer

Dr. Jewel Mullen, Commissioner,  
Department of Public Health,  
State of Connecticut

We have audited the accompanying financial statements of the State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account (State Revolving Fund) (SRF) (an enterprise fund of the State of Connecticut) as of and for the years ended June 30, 2012 and 2011, as listed in the table of contents. These financial statements are the responsibility of the SRF's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with U.S. generally accepted auditing standards 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Clean Water Fund - Drinking Water Federal Revolving Loan Account and do not purport to, and do not, present fairly the financial position of the State of Connecticut, as of June 30, 2012 and 2011, and the changes in its financial position, or, where applicable, its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account - SRF as of June 30, 2012 and 2011, and the changes in its financial position and cash flows thereof for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated September 18, 2012 on our consideration of the State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account - SRF'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 to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Government 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 U.S. generally accepted auditing standards, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

*Seward and Monde*

September 18, 2012

**OFFICE OF THE TREASURER  
STATE OF CONNECTICUT  
DRINKING WATER FUND  
FISCAL YEAR ENDED JUNE 30, 2012  
MANAGEMENT'S DISCUSSION AND ANALYSIS**

This Management Discussion and Analysis (MD&A) of the State of Connecticut Drinking Water Fund provides an introduction to the major activities affecting the operation of the state revolving fund and is a narrative overview of the financial performance for the fiscal year ended June 30, 2012. The information contained in this discussion should be considered in conjunction with the Fund's basic financial statements and the notes thereto.

**Financial Highlights**

Changes in Net Assets - Net assets under management in the Drinking Water Fund at the close of the fiscal year 2012 were \$132,401,515 including assets of \$191,605,650 offset by liabilities of \$59,204,135 compared to fiscal year 2011 were \$125,142,069 including assets of \$189,568,047 offset by liabilities of \$64,425,978. Fund net assets increased by \$7,259,446 or 5.8%.

Net Assets of the Drinking Water Fund are categorized as follows:

Restricted - includes net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.

Unrestricted - includes all net assets that are not restricted and are available for any program purpose. The majority of the net assets are invested and portions are restricted in accordance with the requirements of State Statutes and the Federal Clean Water Act. Restricted assets represent the amount of assets which relate to the federal capitalization grants and associated State match.

The financial statements show restricted fund net assets of \$119,176,974 an increase of \$7,948,499 or 7.15% above the 2011 balance which was adjusted during the year to more closely align with the federal and state restrictions on the Drinking Water Fund.

Loans Receivable - Total loans receivable decreased by \$3,593,806 from \$71,058,367 to \$67,464,561 due to the net of new loans (\$1,698,100) and principal repayments (\$5,291,906).

Bonds Outstanding - During the year, no bonds were issued. The Fund's total debt outstanding decreased by \$4,643,268 to \$55,443,559 as a result of scheduled debt repayments.

Operating Revenues - The Fund's gross operating revenue decreased \$58,208 or 3.5% to \$1,594,996.

Statement of Cash Flows - The Statement of Cash Flows shows a decrease in cash for the year of \$585,461.

Capitalization Grants - During the year, \$5,918,106 was drawn from the U.S. Environmental Protection Agency (US EPA) for projects, compared to \$15,764,103 in 2011. To date, since inception, the State has drawn \$124,793,412. Cumulative federal drinking water capitalization grant awards totaled \$149,917,900. The State has provided the required 20% match of the capitalization grant of \$40,677,637. The match has been provided by the State and used for program purposes in accordance the State's operating agreement with the US EPA.

## **Overview of the Financial Statements**

The Drinking Water Fund financial statements are prepared by the Office of the Treasurer in conjunction with the Department of Public Health (DPH). The Treasurer is responsible for reporting the detailed financial information in the Drinking Water Fund financial statements, which incorporates information, generated and prepared by the DPH Business Office and DPH Drinking Water Section.

The Drinking Water Fund is a part of the Clean Water Fund which is classified as an enterprise fund within the Proprietary Funds of the State of Connecticut. Proprietary Funds focus on the determination of the change in fund net assets, financial position, and cash flow for governmental activities that operate similar to a commercial enterprise. Proprietary funds use the accrual basis of accounting.

The Statements of Revenues, Expenses and Changes in Fund Net Assets divide the activities of the Fund into two categories:

Operating Activities, including the Drinking Water State Revolving Fund project financing program (the Loan Program); and

Nonoperating Activities, including the revenue bonds issued for the Fund (the Revenue Bond Program) and the investment of the Drinking Water State Revolving Fund assets.

For the Loan Program activities, the financial statements indicate the amount of loans financed and the amount of repayments collected during the past year. Fund financial statements also provide information about activities of the Fund as a recipient of federal capitalization grants and state matching funds. The amount of capitalization grants remaining for future use is disclosed in the Notes to the Financial Statements.

The Revenue Bond Program is the leveraged financing strategy implemented by the Connecticut Clean Water Fund that maximizes the financing capacity of the respective federal capitalization grants, the required 20% state match for these grants and the Fund's assets. Based on this strategy, the Connecticut Clean Water Fund issues revenue bonds and uses the proceeds to provide financing for Clean Water and Drinking Water projects. Where necessary, due to the issuance of bonds and investment activities for both the Clean Water Fund and Drinking Water Fund, bond proceeds, interest income and expenses may be allocated between the Clean Water Fund and the Drinking Water Fund. For the Revenue Bond Program activities, the financial statements indicate the amount of the bonds issued and retired, and the remaining amount of bonds to be repaid in the future.

The financial statements indicate the amount of interest income generated by the investment of funds and describe the structure of the investments.

Since 2001, the proceeds of the Connecticut Clean Water Fund bonds have been used for both clean water and drinking water projects. All of the currently outstanding bonds were issued under the 2002 general bond resolution as further described in Notes to the Financial Statements. All of the accounts established under the 2002 general bond resolution, whether restricted or unrestricted, are held by US Bank (the Trustee), as further described in the Notes to the Financial Statements.

## **Operating Activities**

### **The Drinking Water Loan Program**

Loans are made to public water systems, owned by both municipalities and private entities, for project funding. There are two categories of loans, construction loans or interim funding obligations (IFOs) and the long-term permanent financing obligations (PLOs) which are signed after projects are completed. The PLOs have 20 year repayment terms and can be prepaid at any time without penalty. Although there are no state grants available to participants in this program, portions of the federal capitalization grant and the 2009 ARRA funding are used to subsidize the projects.

Construction loans in progress totaled \$39,737 a decrease of \$5,185,034. Payments to public water systems for ongoing projects totaled \$1,698,100. Completed projects which were permanently financed during the year totaled \$6,640,936. There were 5 loan originations during the year.

At year-end there are no delinquent loans in the Drinking Water loan program. Further details about the loans can be found in the Notes to the Financial Statements.

New construction loan commitments totaled \$20,956,159.

Loan repayment collection services are provided by the Trustee, US Bank. Repayments on all DWF loans made by the State since 1998 are paid to the Drinking Water Fund account held at US Bank. These funds provide security for the Bonds and any new Bonds issued hereafter.

## **Non-Operating Activities**

### **Investment of Funds**

The federal capitalization grants and state provided matching funds are used to provide leveraged financing for eligible projects in the state Federal capitalization grants and the match are deposited into the State Revolving Fund accounts held by the Trustee in the form of either cash or permitted investments. State contributions are held by the Trustee in the form of cash, permitted investments or State general obligation bonds and are used as they are deposited for program purposes.

The State currently invests in the State's Short Term Investment Fund (STIF) and in guaranteed investment agreements with financial institutions. The 2002 bond resolution requires that the investment agreements be with, or be guaranteed by, institutions with ratings in the two top rating categories given by Standard & Poor's and Moody's Investors Service or any rating service recognized by the State Banking Commissioner. Certain moneys currently held in the Fund are invested pursuant to investment agreements with AA providers which are collateralized with securities issued or guaranteed by the U.S. Government or agencies or instrumentalities whose market value is at least 100% of the funds invested.

### **The Bond Program**

The Connecticut Clean Water Fund has issued long-term debt obligations backed by the pledge of specific assets including loans, reserve funds and other program assets. Pursuant to the 2002 bond resolution and the State Act, the long-term debt obligations of the Fund are special obligations of the State which are payable only from the revenues or monies available in the Fund. Currently, bonds are outstanding under the 2002 General Revenue Bond Resolution the latest of three resolutions used for Connecticut Clean Water Fund bonds issues since 1991. Proceeds have been used for program purposes including the funding of loans to Drinking Water Fund borrowers. During the year, the state did not issue bonds for new projects. Further information about outstanding bonds can be found in the Notes to the Financial Statements.

The issuance of bonds under the 2002 general bond resolution resulted in the creation of three additional fund accounts. These accounts are the Senior Sinking Fund and the Support Fund which are restricted accounts and the General Revenue Revolving Fund account which is unrestricted. All three accounts are held by the Trustee.

The program's advisors are:

Bond Counsel - Edwards, Angell, Palmer and Dodge and Hardwick Law Firm, LLC

Financial Advisors - Lamont Financial Services Corporation and First Southwest

Trustee - US Bank

Loan Repayment Collection Services - US Bank

Verification Agent - AMTEC

Arbitrage Rebate Calculation Services - AMTEC

Auditor - Seward & Monde CPAs

General Counsel - Attorney General of the State of Connecticut

### **Credit Ratings**

The Connecticut Clean Water Fund is the recipient of credit ratings from three nationally recognized credit rating agencies as follows: AAA from Standard and Poor's, AAA from Fitch Investors Services and Aaa from Moody's' Investor Services.

## SELECTED FINANCIAL INFORMATION

	2012	2011	Increase (Decrease)
Loans Outstanding - current and long term portions	\$67,464,561	\$71,058,367	(\$3,593,806)
Change in Net Assets	\$7,259,446	\$15,413,175	(\$8,153,729)
Operating Revenues – Interest on Loans	\$ 1,594,996	\$ 1,653,204	(\$ 58,208)
Operating Expenses - Less grants to recipients	\$ 4,126,245	\$ 4,176,175	(\$49,930)
Interest on Investments	\$ 1,123,590	\$ 1,220,142	(\$ 96,552)
Interest Expense	\$3,058,622	\$ 2,438,374	\$ 620,248
Federal Capitalization Grants	\$ 6,703,602	\$ 14,845,660	(\$8,142,058)

## ECONOMIC CONDITIONS AND OUTLOOK

As the nation continues to experience slow and erratic growth, Connecticut has maintained persistent focus on economic development and job creation. Like other states, Connecticut has dealt with budget deficits with various strategies while continuing to plan and implement programs designed to bring a variety of manufacturing, technology and research companies to the State. Some recovery continued during fiscal year 2012, however volatility in the jobs numbers hampered the State's ability to reduce unemployment and the unemployment rate at June 2012 was 8.1 percent. Some optimism might be warranted however since consumers are spending again, many businesses are flush with cash, and firms have begun to hire new workers. While home prices have not yet recovered ground lost in 2008 and 2009, sales have begun to pick up pace.

Although the State's economic and financial situation continued to slowly improve, there was a modest budget deficit by the end of the fiscal year, and concern continued about Connecticut's debt levels despite several mitigating factors including Connecticut's ranking highest in per capita income, legislative approval of additional funding for the State employee's Retirement Plan, and expectations of job growth over the next year.

With its diversified economy, measures to spur economic growth will mean continued need for transportation and water infrastructure upgrades and energy improvements. The Drinking Water Fund has made significant efforts to get necessary funding to as many communities as possible. Local, state and federal budget constraints will continue to mean greater pressure on the Fund to provide timely and innovative financial assistance for critical projects. These constraints might be even greater in 2013 if ominous threat of the approaching "fiscal cliff" (the end of the "Bush" tax cuts, payroll tax holiday, and extended unemployment benefits end, and automatic budget cuts) becomes real. All of these factors impact how Connecticut public water systems plan and implement the capital projects funded by the Drinking Water Fund.

The major focus for the Drinking Water Fund continues to be setting priorities and providing financing for critical work, especially for small water systems. The Connecticut Department of Public Health and the Office of the Treasurer, working together, will continue to assist state legislators and public water systems in determining the most cost effective and efficient way to meet their water quality needs.

The Office of the Treasurer Debt Management Division continually monitors the impact of credit ratings of investment providers and municipalities, assists in the preparation of comments on financial regulation and participates in industry discussions on infrastructure, including water and transportation, as well as the economic development and growth potential for the state.

## **REQUIRED SUPPLEMENTARY INFORMATION**

The Drinking Water Fund does not separately report required supplementary information that contains budgetary comparison schedules; schedules presenting infrastructure assets or supplementary pension fund information because this information is recorded by the State of Connecticut.

The Notes to the Financial Statements provide additional information that further explains and supports the information in the financial statements. The Notes provide additional information that is essential to a full understanding of the data provided in the Drinking Water Fund's financial statements.

## **CONTACTS**

This financial report is designed to provide a general overview of the Drinking Water Fund's finances. Questions about this report or requests for additional information should be addressed to:

Drinking Water Fund Financial Administrator  
Connecticut State Treasurer's Office  
Debt Management Division  
55 Elm Street  
Hartford, CT 06106-1773  
Telephone (860) 702-3134  
[www.state.ct.us/ott](http://www.state.ct.us/ott)

Questions about the Drinking Water Fund and water quality in Connecticut should be addressed to:

Connecticut Department of Public Health  
Drinking Water Section  
410 Capitol Avenue, MS# 51 WAT  
P.O. Box 340308  
Hartford, CT 06134-0308  
Telephone (860) 509-7333  
[www.state.ct.us/dph](http://www.state.ct.us/dph)

**STATE OF CONNECTICUT CLEAN WATER FUND -  
DRINKING WATER FEDERAL REVOLVING LOAN ACCOUNT  
(STATE REVOLVING FUND)  
BALANCE SHEETS  
June 30, 2012 and 2011**

	2012	2011
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 7,623,939	\$ 8,209,400
Interest receivable - investments	233,923	252,452
Interest receivable - loans	8,380	117,327
Grant receivable	309,108	-
Loans receivable	4,895,759	9,800,511
Total current assets	13,071,109	18,379,690
Noncurrent assets:		
Loans receivable	62,568,802	61,257,856
Revolving fund	47,396,919	40,338,420
Deferred loss on early retirement of bonds	917,851	1,404,148
Restricted assets:		
Bond proceeds fund	11,361,131	12,953,961
Revolving fund	15,364,574	16,498,805
Debt service fund	31,348,099	28,539,381
Support fund	9,577,165	10,195,786
Total restricted assets	67,650,969	68,187,933
Total noncurrent assets	178,534,541	171,188,357
Total assets	\$ 191,605,650	\$ 189,568,047
<b>LIABILITIES</b>		
Current liabilities:		
Interest payable on revenue bonds	\$ 882,649	\$ 700,891
Deferred grant revenue	-	476,388
Bonds payable	4,951,563	4,643,268
Total current liabilities	5,834,212	5,820,547
Noncurrent liabilities:		
Premium on revenue and refunding bonds	2,877,927	3,161,872
Bonds payable	50,491,996	55,443,559
Total noncurrent liabilities	53,369,923	58,605,431
Total liabilities	59,204,135	64,425,978
<b>FUND NET ASSETS</b>		
Unrestricted	13,224,541	13,913,594
Restricted for loans	119,176,974	111,228,475
Total fund net assets	132,401,515	125,142,069
Total liabilities and fund net assets	\$ 191,605,650	\$ 189,568,047

The notes to the financial statements are an integral part of this statement.

**STATE OF CONNECTICUT CLEAN WATER FUND -  
DRINKING WATER FEDERAL REVOLVING LOAN ACCOUNT  
(STATE REVOLVING FUND)  
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS  
For the Years Ended June 30, 2012 and 2011**

	<u>2012</u>	<u>2011</u>
<b>OPERATING REVENUES</b>		
Interest on loans	\$ 1,594,996	\$ 1,653,204
<b>OPERATING EXPENSES</b>		
Salaries	1,747,222	1,978,007
Employee benefits	1,161,445	1,308,890
Other	1,217,578	889,278
Project grants	906,252	4,626,212
Total operating expenses	<u>5,032,497</u>	<u>8,802,387</u>
Operating loss	<u>( 3,437,501)</u>	<u>( 7,149,183)</u>
<b>NONOPERATING REVENUES (EXPENSES)</b>		
Interest on investments	1,123,590	1,220,142
Amortization of bond premium	283,945	217,017
Interest expense	<u>( 3,058,622)</u>	<u>( 2,438,374)</u>
Total nonoperating revenues (expenses)	<u>( 1,651,087)</u>	<u>( 1,001,215)</u>
Loss before federal capitalization grants and transfers	<u>( 5,088,588)</u>	<u>( 8,150,398)</u>
<b>FEDERAL CAPITALIZATION GRANTS</b>		
Project funds - loans	1,698,100	6,050,344
Project funds - grants	906,252	4,626,212
Set-aside activities	4,099,250	4,169,104
Total federal capitalization grants	<u>6,703,602</u>	<u>14,845,660</u>
<b>OPERATING TRANSFERS</b>	<u>5,644,432</u>	<u>8,717,913</u>
Change in fund net assets	7,259,446	15,413,175
<b>FUND NET ASSETS, beginning</b>	<u>125,142,069</u>	<u>109,728,894</u>
<b>FUND NET ASSETS, ending</b>	<u>\$ 132,401,515</u>	<u>\$ 125,142,069</u>

The notes to the financial statements are an integral part of this statement.

**STATE OF CONNECTICUT CLEAN WATER FUND -  
DRINKING WATER FEDERAL REVOLVING LOAN ACCOUNT  
(STATE REVOLVING FUND)  
STATEMENTS OF CASH FLOWS  
For the Years Ended June 30, 2012 and 2011**

	2012	2011
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Interest received on loans	\$ 1,703,943	\$ 1,583,089
Loan originations	( 1,698,100)	( 6,026,395)
Principal paid on loans receivable	5,291,906	4,453,482
Payments to employees for salaries and benefits	( 2,908,667)	( 3,286,897)
Payments on project grants	( 906,252)	( 4,626,212)
Other payments	( 1,217,578)	( 889,278)
Net cash provided (used) by operating activities	265,252	( 8,792,211)
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>		
Federal capitalization grants	5,918,106	15,764,103
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>		
Repayment of bonds payable	( 4,643,268)	( 4,055,406)
Proceeds from bonds payable	-	16,464,150
Premium on bonds payable	-	1,535,850
Payment to refunded revenue bond escrow agent	-	( 7,281,610)
Interest paid on bonds payable	( 2,390,567)	( 2,140,858)
Operating transfers	5,644,432	8,717,913
Net cash provided (used) by noncapital financing activities	( 1,389,403)	13,240,039
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Interest received on investments	1,142,119	1,234,165
Decrease (increase) in revolving fund	( 7,058,499)	2,809,528
Decrease (increase) in restricted assets	536,964	( 16,460,560)
Net cash used by investing activities	( 5,379,416)	( 12,416,867)
Net change in cash and cash equivalents	( 585,461)	7,795,064
<b>CASH AND CASH EQUIVALENTS, beginning</b>	8,209,400	414,336
<b>CASH AND CASH EQUIVALENTS, ending</b>	\$ 7,623,939	\$ 8,209,400
<b>RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>		
Operating loss	(\$ 3,437,501)	(\$ 7,149,183)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Changes in assets and liabilities:		
Decrease (increase) in interest receivable - loans	108,947	( 70,115)
Decrease (increase) in loans receivable	3,593,806	( 1,572,913)
Net cash provided (used) by operating activities	\$ 265,252	(\$ 8,792,211)

The notes to the financial statements are an integral part of this statement.

STATE of CONNECTICUT CLEAN WATER FUND - DRINKING WATER  
FEDERAL REVOLVING LOAN ACCOUNT (STATE REVOLVING FUND)  
NOTES to FINANCIAL STATEMENTS  
June 30, 2012 and 2011

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1 - NATURE OF ORGANIZATION

The State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account (State Revolving Fund or SRF), an enterprise fund of the State of Connecticut, established in 1998 pursuant to Connecticut General Statutes Section 22a-475 to 22a-483, provides assistance to the public water systems in Connecticut to finance the costs of infrastructure needed to achieve or maintain compliance with the Safe Drinking Water Act (SDWA). The SRF is funded through revenue bonds and federal grants as established under the SDWA, which requires the State of Connecticut (State) to match federal funds to the extent of 20% of federal funds received.

2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the SRF conform to U.S. generally accepted accounting principles as applicable to government enterprises. The following is a summary of the SRF's significant accounting policies:

Basis of Accounting

The financial statements are prepared using the accrual basis of accounting and the flow of economic resources as specified by the Governmental Accounting Standards Board's (GASB) requirements for an enterprise fund.

Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Operating and Nonoperating Revenues and Expenses

The SRF's principal operation consists of making low interest loans and grants to public water systems in Connecticut. Operating revenue consists of interest earned on those loans. Operating expenses consist of personnel, other expenses and grants incurred in the initial approval, disbursement and ongoing servicing of these loans and grants and incurred in set-aside activities.

Nonoperating revenues include interest earned on investments and nonoperating expenses include interest expense on revenue and refunding bonds.

### Revenue Recognition

Federal capitalization grants are reported as nonoperating revenue and are recognized as federal funds are drawn and as the SRF expenditures are made.

### Cash and Cash Equivalents

For purposes of the statements of cash flows, the SRF considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. However, the SRF's policy is to exclude restricted assets from cash and cash equivalents for purposes of the statements of cash flows due to the limitations imposed on their use by the Clean Water Fund Revenue Bond Program General Bond Resolution, adopted by the State Bond Commission on December 17, 2002 (the "Resolution").

### Investments

The SRF's policy is to present all investments at fair value except for money market investments and investment contracts, which the SRF has elected to report at amortized cost. The fair value of investments traded on public markets is determined using quoted market prices. The fair value of state general obligation bonds, which are not traded on a public market, is estimated using a comparison of other State general obligation bonds. Based on this comparison, the cost or par value of the state general obligation bonds approximates their estimated fair value.

There were no material investment gains or losses for the years ended June 30, 2012 and 2011.

### Loans, Allowance for Loan Losses and Credit Risk

The SRF makes loans to public water systems in the State of Connecticut to finance the costs of infrastructure needed to achieve or maintain compliance with the SDWA. Interest rates on the loans range from 2.00% to 4.68% and interest income is recognized as it is earned. The loans are secured by the full faith and credit or revenue pledges of the public water systems, or both. No allowance for loan losses is considered necessary based on management's evaluation of the collectability of the loans. The evaluation takes into consideration such factors as changes in the size of the public water system loans, overall quality, review of specific problem loans, and current economic conditions and trends that may affect the borrowers' ability to pay.

### Restricted Assets

Restricted assets consist of investments, which are segregated into funds and accounts in accordance with the Resolution as previously described, plus amounts determined to be prudent by management including amortizing long-term investments. The Resolution restricts investments to: a) the State Treasurer's Short-Term Investment Fund, b) Tax Exempt Proceeds Fund of the State, c) interest bearing time deposits held by the trustee, a member bank of the Federal Reserve System, or a bank which is insured by

the Federal Deposit Insurance Corporation and d) Investment Obligations as defined in the Resolution.

Bond Premiums/Deferred Loss

The premiums on the revenue and refunding bonds are being amortized over the term of the bonds on a straight-line basis, which yields results equivalent to the interest method.

The deferred loss on early retirement of bonds (Note 8) is being amortized over the shorter of the life of the refunded or refunding bonds.

Revenue Bonds

The following funds and accounts have been established in accordance with the Resolution adopted December 17, 2002:

Fund/Account	Description and Use
Revolving Fund	The Revolving Fund consists of amounts in the water pollution control federal revolving loan account and drinking water federal revolving loan account. The State maintains the Revolving Fund in accordance with the Federal Act. The State shall transfer to the Debt Service Fund any amounts necessary, together with any amounts on deposit therein, sufficient to pay principal of, redemption premium, if any, and interest on bonds.
Bond Proceeds Fund	Receives proceeds from the sale of revenue bonds as specified and determined by the Resolution. Funds are expensed for purposes of financing loans to borrowers under the State Revolving Fund program and if other monies are not available, payment of principal and interest on bonds.
Debt Service Fund	Receives amount from the Revolving Fund, Support Fund and, if necessary, Bond Proceeds Fund sufficient to pay the debt service on the bonds. Pays principal and interest on outstanding bonds.
Support Fund	The Support Fund, and accounts therein, shall be funded in the amounts and in the manner set forth in a Supplemental Resolution. Monies in the Support Fund shall be transferred to the Debt Service Fund to pay the interest, principal and Sinking Fund Installments and Redemption Price due on bonds, in accordance with the schedule set forth in the applicable Supplemental Resolution.
Administrative Fund: Cost of Issuance Account	Established outside the SRF, receives a portion of the revenue bond proceeds. Investment income is transferred to the revenue fund for debt service payments. Used to pay issuance cost on revenue bonds.
Rebate Fund	Receives any earnings required to be rebated to the United States pursuant to the Tax Regulatory Agreement. Used for IRS obligations as required.

## Fund Net Assets

Fund net assets are classified in the following categories:

- a. Invested in Capital Assets, Net of Related Debt - Consists of capital assets including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. The SRF does not have capital assets.
- b. Restricted Net Assets - Consists of net assets with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws or regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- c. Unrestricted Net Assets - All other net assets that do not meet the definition of restricted or invested in capital assets, net of related debt.

## Reclassifications

Certain prior year amounts have been reclassified for comparative purposes.

## Subsequent Events

The SRF has evaluated subsequent events for the period after June 30, 2012 through September 18, 2012, the date the financial statements were available to be issued.

## 3 - CASH DEPOSITS AND INVESTMENTS

According to GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, the SRF needs to make certain disclosures about deposits and investment risks that have the potential to result in losses. Thus, the following deposit and investment risks are discussed below:

Interest Rate Risk - the risk that changes in interest rates will adversely affect the fair value of an investment.

Credit Risk - the risk that an issuer or other counterparty to an investment will not fulfill its obligation.

Concentration of Credit Risk - the risk of loss attributed to the magnitude of an investment with a single issuer.

Custodial Credit Risk (deposits) - the risk that, in the event of a bank failure, the SRF's deposits may not be recovered.

Custodial Credit Risk (investments) - the risk that, in the event of a failure of the counterparty, the SRF will not be able to recover the value of investments or collateral securities that are in the possession of an outside party.

### Cash and cash equivalents

Cash and cash equivalents of the SRF include funds held by the Connecticut State Comptroller and US Bank (Trustee).

As of June 30, 2012 and 2011 funds held by the State Comptroller were \$7,736,627 and \$7,773,047, respectively. These funds are included with other State of Connecticut accounts, and custodial credit risk cannot be determined at the SRF level. As of June 30, 2012 and 2011, the Trustee held cash included in restricted assets in the amount of \$267,742 and \$12,000, respectively.

As of June 30, 2012 funds held in Connecticut Short Term Investment Funds (STIF) were \$89,582,862, of which \$11,361,131 is included in the bond proceeds fund, \$47,396,919 is included in the revolving fund and \$30,824,812 is included in the debt service fund on the Balance Sheet. As of June 30, 2011 funds held in STIF were \$81,243,827, of which \$12,953,961 is included in the bond proceeds fund, \$40,338,420 is included in the revolving fund and \$27,951,446 is included in the debt service fund on the Balance Sheet. STIF is a money market investment pool, rated AAAM as of June 30, 2012 by Standard and Poor's, in which the State, municipal entities, and political subdivisions of the State are eligible to invest. The State Treasurer with the advice of the Investment Advisory Council, whose members include outside investment professionals and pension beneficiaries, establishes investment policies and guidelines. The State Treasurer is authorized to invest STIF funds in U.S. government and agency obligations, certificates of deposit, commercial paper, corporate bonds, savings accounts, bankers' acceptances, repurchase agreements, asset-backed securities, and student loans.

As of June 30, 2012 funds held in Fidelity Institutional Government Money Market (FIGMM) were \$255,545 which is included in the debt service fund on the Balance Sheet. As of June 30, 2011 funds held in FIGMM were \$575,935 which is included in the debt service fund on the Balance Sheet. FIGMM is a money market investment pool, managed by Fidelity Investments, normally investing at least 80% of assets in U.S. Government securities and repurchase agreements for those securities and generally maintaining a dollar-weighted average maturity of 60 days or less.

## Investments

As of June 30, 2012, the SRF had the following investments and maturities:

Investment Type	Fair Value	Investment Maturities (in years)				Rating
		Less than 1	1 - 5	6 - 10	More than 10	
Guaranteed Investment Contracts	\$ 6,529,125	\$ -	\$ -	\$ 6,529,125	\$ -	Aaa
Guaranteed Investment Contracts	5,718,877	-	-	2,573,368	3,145,509	AA+
Guaranteed Investment Contracts	547,988	-	-	-	547,988	A-
U.S. Treasury State & Local Governments	5,883,668	1,246,585	4,567,704	-	69,379	A2
Connecticut General Obligation Bonds	6,262,081	-	-	6,262,081	-	AA
	<u>\$ 24,941,739</u>	<u>\$ 1,246,585</u>	<u>\$ 4,567,704</u>	<u>\$ 15,364,574</u>	<u>\$ 3,762,876</u>	

As of June 30, 2011, the SRF had the following investments and maturities:

Investment Type	Fair Value	Investment Maturities (in years)				Rating
		Less than 1	1 - 5	6 - 10	More than 10	
Guaranteed Investment Contracts	\$ 7,163,698	\$ -	\$ -	\$ 7,163,698	\$ -	Aaa
Guaranteed Investment Contracts	5,902,096	-	-	-	5,902,096	AA+
Guaranteed Investment Contracts	724,848	-	-	-	724,848	A
U.S. Treasury State & Local Governments	6,142,209	258,542	5,526,159	288,129	69,379	Unrated
Connecticut General Obligation Bonds	6,761,740	-	-	-	6,761,740	AA
	<u>\$ 26,694,591</u>	<u>\$ 258,542</u>	<u>\$ 5,526,159</u>	<u>\$ 7,451,827</u>	<u>\$ 13,458,063</u>	

### Interest Rate Risk

The SRF's policy for managing interest rate risk is to have the maturity or redemption dates of investments coincide as nearly as practicable with the times at which funds will be required for purposes as established in the General Bond Resolutions.

### Credit Risk

The SRF minimizes exposure to this risk by investing in Investment Obligations as defined by the Resolution.

### Concentration of Credit Risk

The SRF currently invests approximately 51% and 52%, at June 30, 2012 and 2011, respectively, in long-term investment agreements with Natixis Funding Corp., Trinity Plus Funding and Bank of America.

#### 4 - LOANS RECEIVABLE

The SRF loans funds to qualified public water systems. Principal and interest payments on loans are payable over a 20 year period in equal monthly installments commencing one month after the scheduled completion date, or in a single annual installment representing the first year's principal and interest not later than one year after the scheduled completion date and thereafter in monthly installments. Prepayments are not subject to any penalty.

Loans receivable by type are as follows as of June 30:

	<u>2012</u>	<u>2011</u>
Construction in process	\$ 39,737	\$ 5,224,771
Completed projects	<u>67,424,824</u>	<u>65,833,596</u>
	<u>\$ 67,464,561</u>	<u>\$ 71,058,367</u>

Aggregate maturities of loans receivable in subsequent years for completed projects are as follows:

<u>Year ending June 30</u>	
2013	\$ 4,856,022
2014	4,906,803
2015	4,958,802
2016	5,012,050
2017	5,053,441
Thereafter	<u>42,637,706</u>
	<u>\$ 67,424,824</u>

## 5 - FEDERAL LETTER OF CREDIT

The following represents a summary of the cumulative amounts of funds awarded and drawn, as well as the amount of funds available under the U.S. Environmental Protection Agency's letter of credit as of June 30:

	<u>2012</u>	<u>2011</u>
Awarded	\$ 130,417,900	\$ 130,417,900
Drawn	<u>105,920,909</u>	<u>102,415,716</u>
Available federal letter of credit	<u>\$ 24,496,991</u>	<u>\$ 28,002,184</u>

As part of the State grant agreements with EPA and in accordance with State and Federal statutes, the State is required to provide a 20% match on all federal grant drawdowns. As of June 30, 2012 and 2011, the required State match was \$33,143,713 and \$31,361,627, respectively. As of June 30, 2012 and 2011, the State match provided was \$40,677,637 and \$34,427,239, respectively.

The following represents a summary of the cumulative amount of funds awarded and drawn under the American Recovery and Reinvestment Act of 2009 (ARRA) award as of June 30:

	<u>2012</u>	<u>2011</u>
Awarded	\$ 19,500,000	\$ 19,500,000
Drawn	<u>18,872,503</u>	<u>16,413,654</u>
Available federal letter of credit	<u>\$ 627,497</u>	<u>\$ 3,086,346</u>

## 6 - RESTRICTED ASSETS

Restricted assets as of June 30 are comprised of the following:

	<u>2012</u>	<u>2011</u>
Cash and cash equivalents:		
Money market funds	\$ 42,441,488	\$ 41,481,342
Cash	267,742	12,000
Investments:		
Guaranteed Investment Contracts	12,795,990	13,790,642
U.S. Treasury State and Local Governments	5,883,668	6,142,209
Connecticut General Obligation Bonds	<u>6,262,081</u>	<u>6,761,740</u>
	<u>\$ 67,650,969</u>	<u>\$ 68,187,933</u>

## 7 - RELATED PARTY TRANSACTIONS

The SRF is one fund of many within the State of Connecticut financial reporting structure and as a result, certain transactions including operating transfers, loans receivable and allocation of expenses among funds are under the direction of the State.

### Investments

The SRF has invested in the State Treasurer's Short Term Investment Fund and holds State General Obligation Bonds as presented in Note 3.

### Allocation of Expenses

Fringe benefit costs which are incurred at the State level are applied as a percentage of salaries to all State governmental units, including the SRF. For the years ended June 30, 2012 and 2011, the actual rates were 66.47% and 66.17%, respectively, of the SRF wages and the amounts charged aggregated \$1,161,445 and \$1,308,890, respectively.

## 8 - BONDS PAYABLE

A summary of changes in bonds payable during the year ended June 30, 2012 is as follows:

	Balance June 30, 2011	Issued	Principal Defeasance	Principal Paydown/ Transfers	Balance June 30, 2012
Revenue bonds payable	\$ 55,152,397	\$ -	\$ -	\$ 4,358,124	\$ 50,794,273
Refunding bonds payable	4,934,430	-	-	285,144	4,649,286
	<u>\$ 60,086,827</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 4,643,268</u>	<u>\$ 55,443,559</u>

A summary of changes in bonds payable during the year ended June 30, 2011 is as follows:

	Balance June 30, 2010	Issued	Principal Defeasance	Principal Paydown/ Transfers	Balance June 30, 2011
Revenue bonds payable	\$ 48,788,412	\$ 16,464,150	\$ 6,453,836	\$ 3,646,329	\$ 55,152,397
Refunding bonds payable	5,343,507	-	-	409,077	\$ 4,934,430
	<u>\$ 54,131,919</u>	<u>\$ 16,464,150</u>	<u>-</u>	<u>\$ 4,055,406</u>	<u>\$ 60,086,827</u>

### Revenue Bonds

The proceeds of these bonds are to be used to provide funds to make loans to Connecticut municipalities and public water systems, for use in connection with the financing or refinancing of waste water and drinking water treatment projects.

The State of Connecticut has issued the following bonds, of which a portion has been allocated to the SRF:

Issue Date	Issue Name	Original Allocated Par Amount	Balance Outstanding June 30, 2012
6/1/2001	Clean Water Fund Revenue Bonds, 2001 Series	\$ 29,614,747	\$ -
7/10/2003	State Revolving Fund General Revenue Bonds, 2003 Series A	33,063,800	9,848,123
7/10/2003	State Revolving Fund Refunding General Revenue Bonds, 2003 Series B	7,572,339	4,649,286
7/27/2006	State Revolving Fund General Revenue Bonds, 2006 Series A	5,000,000	3,957,000
8/6/2008	State Revolving Fund General Revenue Bonds, 2008 Series A	25,000,000	16,695,000
6/25/2009	State Revolving Fund General Revenue Bonds, 2009 Series A	4,675,000	4,370,000
3/24/2011	State Revolving Fund General Revenue Bonds, 2011 Series A	16,464,150	15,924,150
		<u>\$ 121,390,036</u>	<u>\$ 55,443,559</u>

The State of Connecticut issued State Revolving Fund General Revenue Bonds 2003 Series dated July 10, 2003 pursuant to the General Bond Resolution adopted December 17, 2002. In accordance with the State Revolving Fund General Revenue Bonds, 2003 Series Plan of Finance, the State allocated the proceeds of 2003 Series Bonds between the SRF and the Clean Water Fund with \$33,063,800 allocated to the SRF and \$85,021,200 allocated to the Clean Water Fund. Debt service on the 2003 Series Bonds is paid from any available monies in the SRF and the Clean Water Fund. The State has pledged amounts in the bond proceeds fund, the support fund and the debt service fund pursuant to the Resolution. After a review of the total expenditures from both programs since 2003, as of July 1, 2006, the State transferred \$10,210,105 in 2003 bond proceeds from the Drinking Water Fund to the Clean Water Fund. An equal principal amount of 2003 bonds will now be designated Clean Water bonds and will be payable from Clean Water revenues for their remaining term. Other related accounts were affected and adjusted to reflect the transfer.

The State of Connecticut issued State Revolving Fund General Revenue Bonds 2006 Series dated July 27, 2006 pursuant to the General Bond Resolution adopted December 17, 2002. In accordance with the State Revolving Fund General Revenue Bonds, 2006 Series Plan of Finance, the State allocated the proceeds of 2006 Series Bonds between the Clean Water Fund and the SRF with \$145,000,000 allocated to the Clean Water Fund and \$5,000,000 allocated to the SRF. Debt service on the 2006 Series Bonds is to be paid from any available monies in the Clean Water Fund and the SRF. The State has pledged amounts in the bond proceeds fund, the support fund and the debt service fund pursuant to the Resolution.

The State of Connecticut issued State Revolving Fund General Revenue Bonds 2008 Series dated August 6, 2008 pursuant to the General Bond Resolution adopted December 17, 2002. In accordance with the State Revolving Fund General Revenue Bonds, 2008 Series Plan of Finance, the State allocated the proceeds of 2008 Series Bonds between the Clean Water Fund and the SRF with \$171,195,000 allocated to the Clean Water Fund and \$25,000,000 allocated to the SRF. Debt service on the 2008 Series Bonds is to be paid from any available monies in the Clean Water Fund and the SRF. The State has pledged amounts in the bond proceeds fund, the support fund and the debt service fund pursuant to the Resolution.

The State of Connecticut issued State Revolving Fund General Revenue Bonds 2009 Series dated June 25, 2009 pursuant to the General Bond Resolution adopted December 17, 2002. In accordance with the State Revolving Fund General Revenue Bonds, 2009 Series Plan of Finance, the State allocated the proceeds of 2009 Series Bonds between the Clean Water Fund and the SRF with \$194,765,000 allocated to the Clean Water Fund and \$4,675,000 allocated to the SRF. Debt service on the 2009 Series Bonds is to be paid from any available monies in the Clean Water Fund and the SRF. The State has pledged amounts in the bond proceeds fund, the support fund and the debt service fund pursuant to the Resolution.

The State of Connecticut issued State Revolving Fund General Revenue Bonds 2011 Series dated March 24, 2011 pursuant to the General Bond Resolution adopted December 17, 2002. In accordance with the State Revolving Fund General Revenue Bonds, 2011 Series Plan of Finance, the State allocated the proceeds of 2011 Series Bonds between the Clean Water Fund and the SRF with \$166,470,850 allocated to the Clean Water Fund and \$16,464,150 allocated to the SRF. Debt service on the 2011 Series Bonds is to be paid from any available monies in the Clean Water Fund and the SRF. The State has pledged amounts in the bond proceeds fund, the support fund and the debt service fund pursuant to the Resolution.

The SRF's revenue bonds payable are serial bonds, of which \$50,794,273 and \$55,152,397 was outstanding as of June 30, 2012 and 2011, respectively. The serial bonds mature through June 1, 2027 and have interest rates ranging from 1.0% to 5.0%.

#### Refunding Bonds - 2003 Series

On July 10, 2003 the State issued \$115,785,000 of State Revolving Fund Refunding General Revenue Bonds, 2003 Series B with interest rates of 2.0% to 5.9% to advance refund Clean Water Fund 2001 Series Revenue Bonds (Refunded Bonds) with a principal balance totaling \$17,834,000 and interest rates of 4.0% to 5.5%. The State allocated \$7,572,339 of the 2003 Series B Refunding Bonds to the SRF. The Refunded Bonds had redemption dates through October 1, 2011.

The net proceeds of the 2003 Series B Refunding Bonds of \$18,879,694 were used to purchase U.S. Government securities and those securities were placed in an irrevocable trust with an escrow agent to provide debt service payments until the Refunded Bonds are called on various dates through October 1, 2011. The advance refunding met the requirements of an in-substance defeasance and, accordingly, the Refunded Bonds with a principal balance of \$17,834,000 were removed from the SRF's balance sheet. As of June 30, 2012 and 2011, the outstanding principal balance of the Refunded Bonds was \$-0- and \$17,834,000, respectively.

The difference of \$1,045,694 between the book value of the Refunded Bonds and the amount deposited to the irrevocable trust to fund their debt service represents a loss which has been deferred and is being recognized as an adjustment of interest expense through June 30, 2016. Amortization of the deferred loss for the years ended June 30, 2012 and 2011 totaled \$321,205 and \$293,129, respectively.

### Cash Defeasance - 2008

On June 30, 2008 the SRF paid \$5,622,931 to advance refund Clean Water Fund 2001 Series Revenue Bonds (Refunded Bonds) with principal balances totaling \$5,514,266 and interest rates of 4.0% to 6.0%. The Refunded Bonds will mature at various dates through October 1, 2012.

The \$5,622,931 was used to purchase U.S. Government securities and those securities were placed in an irrevocable trust with an escrow agent to provide debt service payments and the call premium until the Refunded Bonds are called on various dates through October 1, 2012. The advance refunding met the requirements of an in-substance debt defeasance and, accordingly, the Refunded Bonds with a principal balance of \$5,514,266 were removed from the SRF's balance sheet. As of June 30, 2012 and 2011, the outstanding principal balance of the Refunded Bonds was \$1,393,351 and \$2,816,339, respectively.

The difference of \$7,572 between the book value of the Refunded Bonds and the amount deposited to the irrevocable trust to fund their debt service represents a loss which has been deferred and is being recognized as an adjustment of interest expense through June 30, 2013. Amortization of the deferred loss for the years ended June 30, 2012 and 2011 totaled \$2,944 and \$841, respectively.

### Cash Defeasance - 2011

On March 24, 2011 the SRF paid \$7,281,610 to advance refund Clean Water Fund 2003 Series A Revenue Bonds (Refunded Bonds) with principal balances totaling \$6,453,836 and an interest rate of 5.0%. The Refunded Bonds were scheduled to mature at various dates through October 1, 2019, but have a redemption date of October 1, 2013.

The \$7,281,610 was used to purchase U.S. Government securities and those securities were placed in an irrevocable trust with an escrow agent to provide debt service payments and the call premium until the Refunded Bonds are called on October 1, 2013. The advance refunding met the requirements of an in-substance debt defeasance and, accordingly, the Refunded Bonds with a principal balance of \$6,453,836 were removed from the SRF's balance sheet. As of June 30, 2012 and 2011, the outstanding principal balance of the Refunded Bonds was \$6,453,836.

The difference of \$521,185 between the book value of the Refunded Bonds and the amount deposited to the irrevocable trust to fund their debt service represents a loss which has been deferred and is being recognized as an adjustment of interest expense through June 30, 2014. Amortization of the deferred loss for the years ended June 30, 2012 and 2011 totaled \$162,146 and \$34,746, respectively.

Bond Maturities

Requirements at June 30, 2012 to retire the SRF's revenue and refunding bonds are as follows:

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>
2013	\$ 4,951,563	\$ 2,335,346
2014	5,726,569	2,138,872
2015	5,917,154	1,909,990
2016	6,017,534	1,687,912
2017	5,394,680	1,483,349
2018-2022	16,671,527	4,505,767
2023-2027	10,234,416	1,133,101
2028	530,116	18,433
	<u>\$ 55,443,559</u>	<u>\$ 15,212,770</u>

9 - FUND NET ASSETS

The following represents an analysis of fund net assets for the years ended June 30, 2012 and 2011:

	<u>Unrestricted</u>	<u>Restricted for Loans</u>	<u>Total</u>
Balance at June 30, 2010	\$ 13,377,515	\$ 96,351,379	\$ 109,728,894
Change in fund net assets	<u>536,079</u>	<u>14,877,096</u>	<u>15,413,175</u>
Balance at June 30, 2011	13,913,594	111,228,475	125,142,069
Change in fund net assets	<u>( 689,053)</u>	<u>7,948,499</u>	<u>7,259,446</u>
Balance at June 30, 2012	<u>\$ 13,224,541</u>	<u>\$ 119,176,974</u>	<u>\$ 132,401,515</u>

The fund net assets reserved for loans represents amounts accumulated from federal drawdowns, less set-aside activity expenses not exceeding 31% of the federal grant and subsidies, and the State's match of federal funds.

## 10 - OPERATING TRANSFERS

Operating transfers consist of the following for the years ended June 30:

	<u>2012</u>	<u>2011</u>
Transfers related to CWF debt service	(\$ 605,966)	(\$ 109,774)
State match	1,250,398	1,827,687
Reallocation of funds from CWF	5,000,000	
Interfund transfer from CWF for projects	<u>-</u>	<u>7,000,000</u>
	<u>\$ 5,644,432</u>	<u>\$ 8,717,913</u>

## 11 - LOAN FUNDING COMMITMENTS

The operating agreements for the federal capitalization grants require that the SRF enter into binding commitments with local government units within one year of the receipt of each federal grant payment to provide assistance in an amount equal to 120% (including 20% state matching grants) of each federal capitalization grant.

The following represents a summary of loan commitments at June 30:

	<u>2012</u>	<u>2011</u>
Total funds committed to public water systems	\$ 91,495,470	\$ 90,658,642
Loan amount outstanding to public water systems	<u>67,464,561</u>	<u>71,058,367</u>
Loan commitments outstanding	<u>\$ 24,030,909</u>	<u>\$ 19,600,275</u>

In addition, the SRF has ARRA project grant commitments of \$251,026 and \$1,168,705 as of June 30, 2012 and 2011, respectively.

## 12 - RISK MANAGEMENT

The State of Connecticut is responsible for risk management of the SRF activities through the use of commercial and self-insurance.

# SEWARD AND MONDE

CERTIFIED PUBLIC ACCOUNTANTS  
296 STATE STREET  
NORTH HAVEN, CONNECTICUT 06473-2165  
(203) 248-9341  
FAX (203) 248-5813

## INDEPENDENT AUDITORS' 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*

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Ms. Denise L. Nappier, Treasurer

Dr. Jewel Mullen, Commissioner,  
Department of Public Health,  
State of Connecticut

We have audited the financial statements of the State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account (State Revolving Fund) (SRF) (an enterprise fund of the State of Connecticut) as of and for the year ended June 30, 2012, and have issued our report thereon dated September 18, 2012. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of the SRF is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the SRF's internal control over financial reporting as a basis for designing our auditing procedures 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 SRF's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the SRF's internal control over financial reporting.

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.

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 deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

#### COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the SRF's financial statements are free of 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*.

This report is intended solely for the information and use of the management of the SRF and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

*Seward and Monde*

September 18, 2012

# SEWARD AND MONDE

CERTIFIED PUBLIC ACCOUNTANTS  
296 STATE STREET  
NORTH HAVEN, CONNECTICUT 06473-2165  
(203) 248-9341  
FAX (203) 248-5813

## INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

Ms. Denise L. Nappier, Treasurer

Dr. Jewel Mullen, Commissioner,  
Department of Public Health,  
State of Connecticut

### COMPLIANCE

We have audited the compliance of the State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account (State Revolving Fund) (SRF) (an enterprise fund of the State of Connecticut) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the SRF's major federal programs for the year ended June 30, 2012. The SRF's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of SRF's management. Our responsibility is to express an opinion on SRF's compliance based on our audit.

We conducted our audit of compliance in accordance with U.S. generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133. Those standards and OMB Circular A-133 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 SRF's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the SRF's compliance with those requirements.

In our opinion, the SRF complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on its major federal programs for the year ended June 30, 2012.

## INTERNAL CONTROL OVER COMPLIANCE

Management of SRF is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the SRF's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 SRF'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.

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 deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the management of the SRF and federal awarding agencies and is not intended to be and should not be used by anyone other than these specified parties.

*Seward and Monde*

September 18, 2012

STATE OF CONNECTICUT CLEAN WATER FUND - DRINKING WATER  
 FEDERAL REVOLVING LOAN ACCOUNT (STATE REVOLVING FUND)  
 SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
 For the year ended June 30, 2012

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<u>Federal Grantor; Program Title</u>	<u>Federal CFDA Number</u>	<u>Expenditures</u>
ENVIRONMENTAL PROTECTION AGENCY		
Direct:		
Capitalization Grants for State Revolving Fund	66.468	\$ 4,211,409
Capitalization Grants for State Revolving Fund	ARRA - 66.468	<u>2,492,193</u>
		<u>\$ 6,703,602</u>

See notes to schedule.

STATE OF CONNECTICUT CLEAN WATER FUND - DRINKING WATER  
FEDERAL REVOLVING LOAN ACCOUNT (STATE REVOLVING FUND)  
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
For the year ended June 30, 2012

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A - ACCOUNTING BASIS

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the State of Connecticut Clean Water Fund - Drinking Water Federal Revolving Loan Account (State Revolving Fund) and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of the financial statements.

Revenues are recognized to the extent of expenditures. Expenditures have been recognized to the extent that administrative costs have been incurred by the SRF and charged to the grant and federal funds have been loaned or granted to public water systems during the year.

B - SUBRECIPIENTS

Loans disbursed to subrecipients during year ended June 30, 2012 totaled \$1,698,100, of which \$689,844 were from ARRA grants. Grants disbursed to subrecipients during year ended June 30, 2012 totaled \$906,252, of which \$896,005 were from ARRA grants.

C - MUNICIPAL LOAN BALANCES

The balance of outstanding loans to municipalities totaled \$67,464,561 as of June 30, 2012.

STATE OF CONNECTICUT CLEAN WATER FUND - DRINKING WATER  
 FEDERAL REVOLVING LOAN ACCOUNT (STATE REVOLVING FUND)  
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
 For the year ended June 30, 2012

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SECTION I - SUMMARY OF AUDITORS' RESULTS

Financial Statements

Type of auditors' report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified?      Yes   X   No

Significant deficiency(ies) identified?      Yes   X   None reported

Noncompliance material to financial statements noted?      Yes   X   No

Federal Awards

Internal control over major programs:

Material weakness(es) identified?      Yes   X   No

Significant deficiency(ies) identified?      Yes   X   None reported

Type of auditors' report issued on compliance for major program: Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of Circular A-133?      Yes   X   No

Identification of Major Programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>
66.468	Capitalization Grants for State Revolving Fund
ARRA 66.468	Capitalization Grants for State Revolving Fund

Dollar threshold used to distinguish between type A and type B programs \$ 300,000

Auditee qualified as low risk auditee?   X   Yes      No

SECTION II - FINANCIAL STATEMENT FINDINGS

No findings are reported.

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No findings or questioned costs are reported.