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

AUDIT REPORT

Fiscal Year Ended June 30, 2016

State of South Dakota
Department of Legislative Audit
427 South Chapelle
c/o 500 East Capitol
Pierre, SD 57501-5070

SOUTH DAKOTA BOARD OF WATER AND NATURAL RESOURCES
DRINKING WATER STATE REVOLVING FUND
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STATE OF SOUTH DAKOTA
DEPARTMENT OF LEGISLATIVE AUDIT

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MARTIN L. GUINDON, CPA
AUDITOR GENERAL

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

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 Drinking Water State Revolving Fund, which comprise the statement of net position as of June 30, 2016, and the related statements of revenues, expenses and changes in fund net position, and cash flows for the year then ended, and the related notes to the financial statements, which collectively comprise the Drinking Water State Revolving Fund's basic financial statements, and have issued our report thereon dated October 7, 2016.

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.

Martin L. Guindon, CPA
Auditor General

October 7, 2016

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MARTIN L. GUINDON, CPA
AUDITOR GENERAL

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 Drinking 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, 2016, and the related notes to the financial statements, which collectively comprise the Drinking 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 Drinking Water State Revolving Fund as of June 30, 2016, 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.

Emphasis of Matter

As described in Note 1, the financial statements present only the Drinking Water State Revolving Fund and do not purport to, and do not, present fairly the financial position of the Board of Water and Natural Resources as of June 30, 2016, the changes in its financial position, or, where applicable, its cash flows 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 5-7 and the Schedules of Proportionate Share of the Net Pension Liability (Asset) and Employer Contributions on pages on 19-20 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 October 7, 2016 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

October 7, 2016

MANAGEMENT'S DISCUSSION AND ANALYSIS

This section of the South Dakota Department of Environment and Natural Resources Drinking 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, 2016. 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.

DEBT ADMINISTRATION

The Drinking Water Fund is authorized to issue revenue bonds for the purpose of financing loans and other types of financial assistance to qualified communities or local agencies for drinking water projects.

The Fund's bonds are rated AAA with a positive outlook by Standard and Poor's and Aaa by Moody's Investor Service.

More detailed information about the Authority's debt can be found in Note 4, Long-Term Debt.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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

Changes in Net Position

For the fiscal year ended June 30, 2016, net position of the Fund increased by 9.7% – primarily due to total revenues for the Fund exceeding total expenses by $16,380,841. This increase is larger than the 6.2% increase in FY15 due primarily to federal capitalization grants receipts totaling $6.3 million more in FY16 than in FY15 and a $460,000 increase in investment income. GASB Statement 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. GASB Statement 68 & 71 required that pensions be reported in the Financial Statements. Those amounts are reflected in the Deferred Outflows and Inflows shown in the table below.

NET POSITION

	2016	2015	% Change
Current Assets	$ 49,825,485	$ 44,868,955	11.0%
Noncurrent Assets	200,266,002	193,904,061	3.3%
Total Assets	250,091,487	238,773,016	4.7%
Related To Pensions	96,849	70,247	37.9%
Deferred Amount of Refunding	2,249,877	2,513,541	-10.5%
Total Deferred Outflows of Resources	2,346,726	2,583,788	-9.2%
Current Liabilities	8,427,489	6,927,078	21.7%
Noncurrent Liabilities	58,958,017	65,709,306	-10.3%
Total Liabilities	67,385,506	72,636,384	-7.2%
Related to Pensions	76,637	89,451	-14.3%
Total Deferred Inflows of Resources	76,637	89,451	-14.3%
Net Position:			
Restricted For Pension Benefits	71,700	58,031	23.6%
Unrestricted	184,904,370	168,572,938	9.7%
Total Net Position	$ 184,976,070	$ 168,630,969	9.7%

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

MANAGEMENT'S DISCUSSION AND ANALYSIS

CHANGES IN NET POSITION

	2016	2015	% Change
Loan Interest Income	$ 3,434,320	$ 3,311,988	3.7%
Other Income	899,092	884,959	1.6%
Total Operating Revenue	4,333,412	4,196,947	3.3%
Administrative Expenses	921,442	929,420	-0.9%
Grant Expenses	5,234,593	4,553,346	15.0%
Interest Expense	2,350,250	2,389,349	-1.6%
Bond Issuance Expense	0	69,121	-100.0%
Total Operating Expenses	8,506,285	7,941,236	7.1%
Operating Income (Loss)	(4,172,873)	(3,744,289)	11.4%
Federal Capitalization Grants	17,764,511	11,451,552	55.1%
Other Income	208,983	208,533	0.2%
Investment Income	3,105,522	2,645,194	17.4%
Investment Expense	(1,744)	(5,845)	-70.2%
Arbitrage**	(523,559)	(704,442)	-25.7%
Payments to State	(35,739)	(34,284)	4.2%
Non Operating Rev (Exp)	20,517,974	13,560,708	51.3%
Change in Net Position	16,345,101	9,816,419	66.5%
Beginning Net Position*	168,630,969	158,814,550	6.2%
Total Net Position	$ 184,976,070	$ 168,630,969	9.7%

*2015 was restated in accordance with GASB Statement 68 & 71.
**2016 Arbitrage reclassification was due to recent GASB pronouncements and review of current information.

CURRENT CONDITIONS

The state is challenged demographically with a large number of small rural communities and only two cities with populations over 50,000 people. The Drinking Water State Revolving Fund Program assists the state in meeting these challenges and infrastructure needs. In state fiscal year 2016, the Drinking Water State Revolving Fund obligated $23.6 million to 16 projects.

SOUTH DAKOTA BOARD OF WATER
AND NATURAL RESOURCES
DRINKING WATER STATE REVOLVING FUND
STATEMENT OF NET POSITION
June 30, 2016

Assets		
Current Assets:		
Cash and Cash Equivalents	$	29,817,631.96
Investments		7,469,547.82
Due from Federal Government		245,059.17
Due from Other Governments		206,099.45
Accrued Interest Receivable		2,044,374.26
Loans Receivable		10,042,772.48
Total Current Assets		49,825,485.14
Noncurrent Assets:		
Investments		57,428,643.34
Restricted Net Pension Asset		51,488.00
Loans Receivable		142,785,870.29
Total Noncurrent Assets		200,266,001.63
Total Assets		250,091,486.77
Deferred Outflows of Resources		
Related to Pensions		96,849.00
Deferred Charge on Refunding		2,249,877.38
Total Deferred Outflows of Resources		2,346,726.38
Liabilities		
Current Liabilities:		
Accounts Payable		187,684.63
Accrued Liabilities		17,673.79
Compensated Absences Payable		28,468.13
Accrued Interest Payable		935,036.19
Arbitrage Payable		1,165,559.11
Bonds Payable - net of unamortized premium and discount		6,093,067.18
Total Current Liabilities		8,427,489.03
Noncurrent Liabilities:		
Compensated Absences Payable		25,033.33
Bonds Payable - net of unamortized premium and discount		58,932,983.98
Total Noncurrent Liabilities		58,958,017.31
Total Liabilities		67,385,506.34
Deferred Inflows of Resources		
Related to Pensions		76,637.00
Total Deferred Inflows of Resources		76,637.00
Net Position		
Restricted For Pension Obligations		71,700.00
Unrestricted		184,904,369.81
Total Net Position	$	184,976,069.81

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

SOUTH DAKOTA BOARD OF WATER
AND NATURAL RESOURCES
DRINKING WATER STATE REVOLVING FUND
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET POSITION
For the Fiscal Year Ended June 30, 2016

Operating Revenues:		
Loan Interest Income		$ 3,434,319.94
Other Income		899,092.29
Total Operating Revenue		4,333,412.23
Operating Expenses:		
Administrative Expenses		
Personal Services	240,935.37	
Employee Benefits	53,045.38	
Travel	7,982.74	
Contractual	555,308.65	
Supplies	172.19	
Grants	62,549.02	
Other	1,449.17	
Total Administrative Expenses		921,442.52
Grant Expense		5,234,593.00
Interest Expense		2,350,249.85
Total Operating Expenses		8,506,285.37
Operating Income (Loss)		(4,172,873.14)
Nonoperating Revenue (Expenses):		
Federal Capitalization Grants		17,764,511.46
Other Income		208,983.34
Investment Income		3,105,522.02
Investment Expense		(1,744.02)
Arbitrage Rebate		(523,559.04)
Payments to State		(35,739.34)
Total Nonoperating Revenues (Expenses)		20,517,974.42
Change in Net Position		16,345,101.28
Net Position at Beginning of Year		168,630,968.53
Net Position at End of Year		$ 184,976,069.81

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

SOUTH DAKOTA BOARD OF WATER AND NATURAL RESOURCES
DRINKING WATER STATE REVOLVING FUND
STATEMENT OF CASH FLOWS
For the Fiscal Year Ended June 30, 2016

Cash Flows from Operating Activities:		
Receipts for Loan Repayments	$ 14,372,758.30	
Receipts for Interest Income on Loans	3,266,440.10	
Receipts for Surcharge Interest on Loans	862,084.68	
Payments to Loan Recipients	(24,202,177.00)	
Payments for Employee Services	(300,067.12)	
Payments for Contractual Services	(524,890.13)	
Payment for Grants	(72,000.00)	
Payments for Principal Forgiveness	(5,234,593.00)	
Other Payments	(9,554.10)	
Net Cash Provided (Used) by Operating Activities		(11,841,998.27)
Cash Flows from Noncapital Financing Activities:		
Payments to State	(35,739.34)	
Principal Payments on Bonds	(5,535,000.00)	
Interest Payments on Bonds	(2,307,488.72)	
Receipts for Administering Program	17,759,405.00	
Other Income	208,983.34	
Net Cash Provided (Used) by Noncapital Financing Activities		10,090,160.28
Cash Flows from Investing Activities:		
Arbitrage Payment	(47,134.80)	
Interest on Investments	3,065,723.42	
Proceeds from Sale of Investment Securities	19,481,971.89	
Purchase of Investment Securities	(11,186,795.70)	
Net Cash Provided (Used) by Investing Activities		11,313,764.81
Net Increase (Decrease) in Cash and Cash Equivalents		9,561,926.82
Cash and Cash Equivalents at Beginning of Year		20,255,705.14
Cash and Cash Equivalents at End of Year		$ 29,817,631.96
Reconciliation of Operating Income to Net Cash Provided (Used) by Operating Activities		
Operating Income (Loss)		$ (4,172,873.14)
Adjustments to Reconcile Net Income to Net Cash Provided (Used) by Operating Activities:		
Interest Expense	2,350,249.85	
Bond Issuance Expense		
Assets: (Increase)/Decrease		
Loans Receivable	(9,829,418.70)	
Accrued Interest Receivable on Loans	(167,879.84)	
Due from Other Governments	(37,007.61)	
Pension Assets	25,747.00	
Decrease/(Increase) in Deferred Outflows of Resources:		
Deferred Outflows of Resources - Related to Pensions	(26,602.00)	
Liabilities: Increase/(Decrease)		
Accounts Payable	21,017.54	
Accrued Employee Benefits	8,238.35	
Accrued Liabilities	(655.72)	
Increase/(Decrease) in Deferred Inflows of Resources:		
Deferred Inflows of Resources - Related to Pensions	(12,814.00)	
Total Adjustments		(7,669,125.13)
Net Cash Provided by Operations		$ (11,841,998.27)

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

SOUTH DAKOTA BOARD OF WATER AND NATURAL RESOURCES
DRINKING WATER STATE REVOLVING FUND
NOTES TO THE FINANCIAL STATEMENTS
June 30, 2016

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Authorizing Legislation

The Drinking Water State Revolving Fund (DWSRF) Loan Program was federally authorized by the Safe Drinking Water Act Amendments of 1996. The state authorized the loan program in 1994 in anticipation of federal action. The Environmental Protection Agency (EPA) developed final guidance for the Drinking Water State Revolving Fund on February 28, 1997. The Board of Water and Natural Resources, acting in its capacity as the South Dakota Conservancy District, conducted a public hearing on April 15, 1997 to adopt formal administrative rules for the program. The South Dakota Conservancy District (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 acting in its capacity as the Conservancy District. The DWSRF is a low interest loan program to finance drinking water projects. 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 DWSRF 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 DWSRF 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 except for Guaranteed Investment Contracts, which are non-participating and, therefore, are recorded at carrying value. Unrealized gains and losses due to fluctuations in market value are included in investment income.

F. Premium and Deferred Amount on Refunding

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

G. 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 DWSRF records all revenues derived from interest on loans as operating revenues since these revenues are generated from the DWSRF'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 DWSRF program.

H. 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:	66.468
Federal Agency:	Environmental Protection Agency
Program:	Drinking Water State Revolving Fund
State Agency:	Environment & Natural Resources
Outstanding Loans:	$152,828,643
Current Year	
Administrative Expense:	$738,391
Loan Disbursement:	$29,436,770

I. Reclassifications

Certain reclassifications have been made to the accompanying financial statements based upon recent GASB pronouncements and review of current information. The reclassifications included reporting arbitrage in the Statement of Revenues, Expenses, and Changes in Fund Net Position as nonoperating rather than operating expenses and in the Cash Flows Statement as investing activity rather than operating activity. The reclassifications had no impact on the change in net position or the net position.

J. Net Position

Net Position is classified in the following three components:

- Net investment in capital assets - This component consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any debt that is attributable to the acquisition, construction, or improvement of those assets.
- Restricted- Consists of net position with constraints placed on their use by (1) bond indentures and (2) law through enabling legislation.
- Unrestricted - Consists of net position that does not meet the definition of net investment in capital assets or restricted.

K. Pension

For purposes of measuring the net pension asset, deferred outflows of resources and deferred inflows of resources related to pensions, and pension revenue, information about the fiduciary net position of the South Dakota Retirement System (SDRS) and additions to/deletions from SDRS's fiduciary net position have been determined on the same basis as they are reported by SDRS. Drinking Water SRF contributions and net pension asset are recognized on an accrual basis of accounting.

2. CASH AND INVESTMENTS

Cash

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 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 1.35% for state fiscal year 2016.

Management of the State's internal investment pool is the statutory responsibility of the South Dakota Investment Council (SDIC). The investment policy and required 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.

The Goldman Sachs Fund was rated "AAAm" by Standard and Poor's Rating Group. The fund paid less than .01% for the period 7/01/2015– 6/30/2016. Federated Funds were rated "AAAm by Standard and Poor's Rating Group and paid .07% over the same period.

Investments

Investments must be categorized within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the assets. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

First National Bank (FNB) which serves as trustee to the DWSRF uses a pricing service, Standard and Poor's Security Evaluation (SPSE), to value investments SPSE uses market approach pricing which utilizes models and pricing systems as well as mathematical tools and pricing analyst judgement. All DWSRF investments are priced by this service, which is not quoted prices in the active market, but rather significant other observable inputs; therefore, the investments are categorized as Level 2.

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.

Level 2

Investment	Maturities	Fair Value
US Treasury Bonds	8/31/2016	$ 475,485
US Treasury Bonds	5/31/2017	525,515
US Treasury Bonds	11/30/2016	950,076
US Treasury Bonds	12/31/2016	2,490,641
US Treasury Bonds	10/31/2016	2,500,364
		$ 6,942,081
Federal Agency Bonds	4/27/2017	$ 527,468
Federal Agency Bonds	8/28/2017	145,406
Federal Agency Bonds	12/20/2017	401,440
Federal Agency Bonds	3/07/2018	376,162
		$ 1,450,476

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations to the DWSRF.

Excluding investments explicitly guaranteed by the U.S. Government which are not considered to have credit risk, the DWSRF held Federal Agency Bonds with a fair value of $1,450,476 which were rated Aaa by Moody's Investor Services.

Custodial Credit Risk: Custodial credit risk is the risk that in the event of a bank failure, the Drinking Water State Revolving Fund's investments may not be returned. At June 30, 2016, $56,505,635 of guaranteed investment contracts was uninsured and unregistered, with the securities held by its trust department, but not in the DWSRF's name and, as a result, were exposed to custodial credit risk. Also, investments made in US Treasury Bonds with a market value of $6,942,081 and in Federal Agency Bonds with a market value of $1,450,476 were exposed to custodial credit risk.

Guaranteed Investment Contracts (GICS)

The DWSRF holds the following GICS where the rate of return is guaranteed.

	Maturities	Contract Value
Guaranteed Investment Contract	8/01/2025	$ 43,402,129
Guaranteed Investment Contract	8/01/2026	13,103,506
		$ 56,505,635

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:

Moody's Rating	Contract Value
Baa1	$ 56,505,635

This guarantor's rating is below the acceptable rating category (i.e., below Moody's Aa3). This investment has 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.

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. Loans made from the DWSRF may be made at or below market interest rates and may be fully amortized up to thirty years. Disadvantaged Communities may be eligible for lower rates or even zero percent, and may be fully amortized up to thirty years. Interest rates are reduced for those loans with shorter amortization periods.

4. LONG-TERM DEBT

Revenue Bonds

The bond issues outstanding as of June 30, 2016 are as follows:

Issue	Interest Rate	Maturity Through	Principal Balance
Series 2010AB			
Build America Bonds (BABs)			
Leveraged Term Bonds	4.084% - 5.646%	2031	$ 12,665,000
Tax Exempt Bonds			
Leveraged Term Bonds	2.000% - 5.125%	2030	10,710,000
State Match Term Bonds	2.000% - 5.125%	2030	4,635,000
Series 2012AB			
Taxable Revenue Bonds			
State Match	0.250% - 3.183%	2027	4,250,000
Leveraged	0.250% - 3.183%	2027	18,675,000
Revenue Bonds			
State Match	2.000% - 5.000%	2023	1,505,000
Series 2014A			
Taxable Revenue Bonds			
State Match	0.300% - 1.920%	2020	4,225,000
Series 2014B			
Revenue Bonds			
Leveraged	2.000% - 5.000%	2035	5,770,000
Total			62,435,000
Add: Unamortized Premium			2,591,051
Total Net of Amortization			$ 65,026,051

Future bond payments and future interest payments remaining as of June 30, 2016 are as follows:

Year Ended June 30,	Principal	Interest	Total Principal and Interest
2017	$ 5,925,000	$ 2,174,213	$ 8,099,213
2018	6,075,000	2,022,697	8,097,697
2019	6,255,000	1,853,711	8,108,711
2020	5,850,000	1,684,739	7,534,739
2021	4,215,000	1,537,073	5,752,073
2022-2026	20,465,000	5,403,772	25,868,772
2027-2031	11,965,000	1,849,642	13,814,642
2032-2035	1,685,000	173,875	1,858,875
TOTAL	$ 62,435,000	$ 16,699,722	$ 79,134,722

Changes in long-term liabilities

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Revenue Bonds	$ 67,970,000	$ 0	$ (5,535,000)	$ 62,435,000	$ 5,925,000
Add: Bond Premium	2,759,118	0	(168,067)	2,591,051	168,067
Total	70,729,118	0	(5,703,067)	65,026,051	6,093,067
Compensated Absences	45,263	19,210	(10,972)	53,501	28,468
Long-Term Liabilities	$ 70,774,381	$ 19,210	$ (5,714,039)	$ 65,079,552	$ 6,121,535

5. COMMITMENTS

As of June 30, 2016, the DWSRF had loan commitments with political subdivisions worth $28,399,686.

6. PENSION PLAN

The Department of Environment and Natural Resources, (DENR), 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 contacting the SDRS in writing at South Dakota Retirement System, P.O. Box 1098, Pierre, SD 57501-1098 or by calling (605) 773-3731. Additionally, the State of South Dakota's Comprehensive Annual Financial Report (CAFR) will report the State's proportionate share of the plan. The CAFR can be obtained by writing to the Department of Legislative Audit, 427 South Chapelle, c/o 500 East Capitol, Pierre, South Dakota 57501 or by calling (605)773-3595.

State law requires employees to contribute 6 percent of their salary to the plan and 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. DENR contributions to the SDRS for the fiscal years ended June 30, 2016, 2015, and 2014 were $16,172.26, $15,353.52, and $12,834.14, respectively, equal to the required contributions each year.

The net pension asset was measured as of June 30, 2015 and the SDRS is 104.1% funded. At June 30, 2016, the DWSRF reported an asset of $51,488 for its proportionate share of the net pension asset. For the fiscal year ended June 30, 2016, there was no pension revenue recorded. At June 30, 2016, deferred outflows of resources and deferred inflows of resources related to pensions were reported from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experience	$ 10,542	$ -
Changes in assumption	40,826	-
Net difference between projected and actual earnings on pension plan investments	31,453	75,971
Changes in Proportionate Share		666
Contributions after the measurement date	14,028	-
Total	$ 96,849	$ 76,637

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, 2016, a liability existed for accumulated annual leave calculated at the employee's June 30, 2016 pay rate in the amount of $22,813. 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, 2016 a liability existed for accumulated sick leave, calculated at each employee's June 30, 2016 pay rate in the amount of $30,689. The total leave liability of $53,501 at June 30, 2016 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 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, 5) coverage for property loss through

the South Dakota Property and Casualty Insurance Company, LLC. 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

On 9/2/16 First National Bank provided DENR with written notice of their intent to terminate its consultant contract as Trustee to the State Clean Water and Drinking Water SRF programs. In the notice they stated that the Trust Indenture provides guidance regarding the Trustee's resignation requiring written notice of not less than 30 to days to the Conservancy District and other parties. Furthermore, the Trust Indenture provides that any such resignation or removal shall not take effect until a successor has been appointed, has accepted the duties of Trustee and all funds, property (including any credit enhancement instrument and Liquidity Facilities) have been transferred to the successor. The bank representatives stated their intent to work with DENR to facilitate an orderly transition to a successor trustee. The Conservancy District intends to put out an RFP to select and transition to a new Trustee as soon as possible.

SCHEDULE OF THE DRINKING WATER STATE REVOLVING FUND CONTRIBUTIONS

as of June 30, 2016

South Dakota Retirement System

Last 10 Fiscal Years

	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
Contractually required contribution	$ 13,669	$ 13,296	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Contribtutions in relation to the contractually required contribution	$ 13,669	$ 13,296	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Contribution deficiency (excess)	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
District's covered-employee payroll	$ 241,482	$ 222,624	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Contributions as a percentage of covered-employee payroll	5.66%	5.97%	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -

This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, governments should present information for those years for which information is available.

SCHEDULE OF THE DRINKING WATER STATE REVOLVING FUND'S PROPORTIONATE SHARE OF THE NET PENSION LIABILITY (ASSET)

as of June 30, 2016

South Dakota Retirement System

Last 10 Fiscal Years *

	2016	2015	2014	2013	2012	2011	2010	2009	2008	2007
District's proportion of the net pension liability (asset)	0.05408%	0.04858%	%	%	%	%	%	%	%	%
District's proportionate share of net pension liability (asset)	$ 51,488	$ 77,235	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
District's covered-employee payroll	$ 241,482	$ 222,624	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
District's proportionate share of the net pension liability (asset) as a percentage of its covered-employee payroll	21.32%	34.69%								
Plan fiduciary net position as a percentage of the total pension liability (asset)	104%	107%								

* The amounts presented for each fiscal year were determined as of 06/30

This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, governments should present information for those years for which information is available.