

***RHODE ISLAND CLEAN WATER  
FINANCE AGENCY***

***FINANCIAL STATEMENTS  
FOR THE YEARS ENDED  
JUNE 30, 2005 AND 2004***

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

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## ***INDEPENDENT AUDITOR'S REPORT***

To the Board Members  
Rhode Island Clean Water Finance Agency  
Providence, Rhode Island

We have audited the accompanying financial statements of the RHODE ISLAND CLEAN WATER FINANCE AGENCY, a component unit of the State of Rhode Island and Providence Plantations (State), as of and for the years ended June 30, 2005 and 2004, as listed in the table of contents. These financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the RHODE ISLAND CLEAN WATER FINANCE AGENCY as of June 30, 2005 and 2004, and the changes in financial position and cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated September 19, 2005 on our consideration of the RHODE ISLAND CLEAN WATER FINANCE AGENCY'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 conjunction with this report in considering the results of our audit.

The Management's Discussion and Analysis on pages 3 - 9 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and express no opinion on it.

September 19, 2005

*Cayce Caccia, LLP.*

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**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

The Rhode Island Clean Water Finance Agency (the "Agency") has the pleasure to offer readers of these financial statements this narrative overview and analysis of the financial activities of the Agency for the fiscal year ended June 30, 2005. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues and activities and to identify any significant changes in financial position. The Agency encourages readers to consider the information presented here in conjunction with the financial statements as a whole.

**FINANCIAL HIGHLIGHTS:**

- The Agency's total assets at June 30, 2005 were \$827,899,655, which is an increase of \$127,592,734 or 18.2% over June 30, 2004.
- The Agency's capital assets at June 30, 2005 were \$50,356, which is a decrease of \$7,406 or 12.8% below June 30, 2004.
- The Agency's total operating revenues for the fiscal year ended June 30, 2005 was \$27,098,107, which is an increase of \$6,736,240 or 33.1% over the fiscal year ended June 30, 2004.
- The Agency's operating expenses for the fiscal year ended June 30, 2005 were \$23,603,275, which is an increase of \$4,235,222 or 21.9% over the fiscal year ended June 30, 2004.
- The Agency's total net assets for the fiscal year ended June 30, 2005 was \$291,762,418, which is an increase of \$27,480,185 or 10.4% over the fiscal year ended June 30, 2004.

**2005 FISCAL SUMMARY:**

In other activity, the Agency has assumed \$112,585,000 in new bond indebtedness; however the Agency has created additional assets by issuing new loans to Rhode Island borrowers totaling \$121,190,587.

- December 30, 2004, the Agency issued a \$69,625,000 Series 2004A Bond Issue. This bond issue was part of a total loan pool of \$76,016,300 made to eight borrowers in the Clean Water State Revolving Fund. The following is a list of the borrowers and their loan amount:

Barrington	\$ 4,392,000
Bristol	\$ 1,000,000
Cranston	\$ 3,400,000
Middletown	\$ 2,500,000
NBC Pool # 8	\$40,000,000
Warwick	\$20,000,000
Westerly	\$ 1,724,300
West Warwick	\$ 3,000,000
	<u>\$76,016,300</u>

**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

- August 12, 2004, the Agency issued a Drinking Water loan to New Shoreham in the amount of \$614,287.
- May 6, 2005, the Agency issued a CSSLP loan to the town of Johnston in the amount of \$250,000.
- March 23, 2005, the Agency issued a 2005A Bond Issue in the amount of \$42,960,000. This was part of a total loan pool of \$44,010,000 made to three borrowers in the Drinking Water State Revolving Fund. This was the second time the Agency has gone to the Bond Market to leverage its funds in the Drinking Water Program. The following is a list of the borrowers and their loan amount:

Pawtucket WSB	\$ 31,909,000
Providence WSB	\$ 8,101,000
Woonsocket	\$ 4,000,000
	<u>\$ 44,010,000</u>

- June 13, 2005, the Agency issued a CSSLP loan to the Town of Charlestown in the amount of \$300,000.

**OVERVIEW OF THE FINANCIAL STATEMENTS:**

The Agency's financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied on an accrual basis. Under the accrual basis, revenues are recognized in the period in which they are earned and expenses are recognized in the period in which they are incurred. The three basic financial statements presented within the financial statements are:

Statement of Net Assets – This statement presents information regarding the Agency's assets, liabilities and net assets. Net assets represent the total amount of assets less the total liabilities. The statement of net assets classifies assets, liabilities and net assets as current, non-current and restricted.

Statement of Revenues, Expenses and Changes in Net Assets – This statement presents the Agency's operating revenues, operating expenses and changes in net assets for the fiscal year.

Statement of Cash Flow – The Agency's statement of cash flows is presented on the direct method of reporting, which reflects cash flows from operating, non-capital financing, capital and investing activities.

**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

**FINANCIAL ANALYSIS:**

**NET ASSETS**

The Agency's total net assets at June 30, 2005 was \$291,762,418, which is an increase of \$27,480,185 or 10.4% over June 30, 2004. Components of the Agency's statement of net assets were as follows at June 30:

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Other assets	\$827,849,299	\$700,249,159	\$543,785,478
Capital assets	<u>50,356</u>	<u>57,762</u>	<u>53,115</u>
<b>Total assets</b>	<u>827,899,655</u>	<u>700,306,921</u>	<u>543,838,593</u>
Current liabilities	28,144,002	19,304,891	16,589,888
Non-current liabilities	<u>507,993,235</u>	<u>416,719,797</u>	<u>280,394,697</u>
<b>Total liabilities</b>	<u>536,137,237</u>	<u>436,024,688</u>	<u>296,984,585</u>
<b>Net assets</b>			
Invested in capital assets	50,356	57,762	53,115
Restricted for debt service	279,998,423	255,615,508	240,609,145
Unrestricted	<u>11,713,639</u>	<u>8,608,963</u>	<u>6,191,748</u>
<b>Total net assets</b>	<u><u>\$291,762,418</u></u>	<u><u>\$264,282,233</u></u>	<u><u>\$246,854,008</u></u>

The increases noted above in the Agency's total assets and liabilities are the confirmation of the Agency's steady growth. The 2005 increase results from the Agency closing a \$69.6 million Clean Water bond issue in December, a \$42.96 million Drinking Water bond issue in March. Total assets grew from \$700,306,921 at June 30, 2004 to \$827,899,655 at June 30, 2005. Current liabilities grew from \$19,304,891 at June 30, 2004 to \$28,144,002 or 46% at June 30, 2005. The growth over the past year also relates to non-current liabilities totaling \$507,993,235 which is an increase of \$91,273,438 or 22% over June 30, 2004. The increases noted in unrestricted assets, restricted assets, and non-current liabilities are related to the increase level of loan activity through issuance of bonds.

**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

**CHANGES IN NET ASSETS**

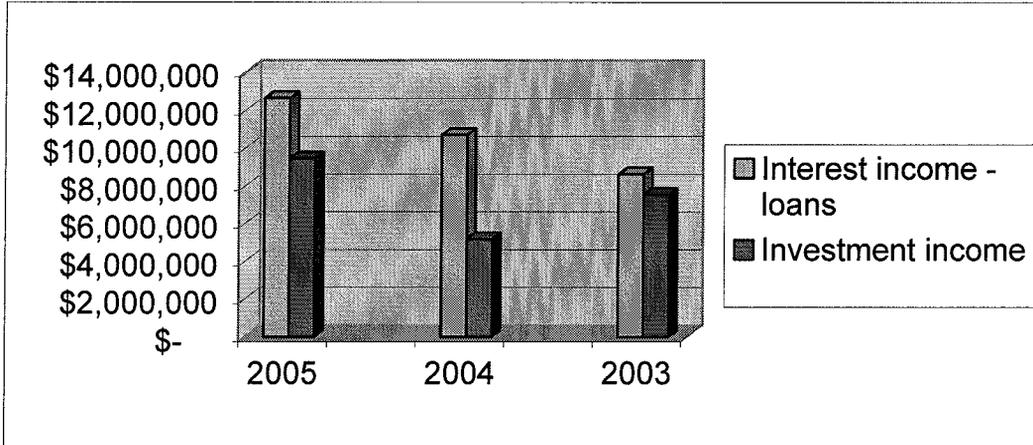
The Agency's change in net assets for the fiscal year ended June 30, 2005 was \$27,480,185. The increase in investment income results from the following: an increase in interest rates on both short and long term investments and unrealized gains on certain investments at June 30, 2005. In 2005 grant income increased due to the maturing of the Drinking Water program, construction draws increased, which caused more federal funds to be drawn, to fund the Local Interest Subsidy Trust (LIST) accounts.

	<u>2005</u>	<u>2004</u>	<u>2003</u>
Interest income - loans	\$ 12,635,671	\$ 10,681,840	\$ 8,618,855
Investment income	9,447,001	5,168,533	7,517,683
Grant income - DEM & DOH	2,349,948	2,272,236	1,449,815
Grant income - federal and state	23,985,353	16,434,411	27,246,160
Other operating revenues	<u>2,665,487</u>	<u>2,239,258</u>	<u>1,558,382</u>
<b>Total income</b>	<u>51,083,460</u>	<u>36,796,278</u>	<u>46,390,895</u>
Interest expense	20,265,522	16,244,743	12,384,791
Other operating expenses:			
Consulting fees :DEM & DOH	2,349,948	2,272,236	1,449,815
General administration	816,457	700,262	613,988
Professional fees	<u>171,348</u>	<u>150,812</u>	<u>140,922</u>
<b>Operating expenses</b>	<u>23,603,275</u>	<u>19,368,053</u>	<u>14,589,516</u>
Increase in net assets	27,480,185	17,428,225	31,801,379
<b>Net assets, beginning of year</b>	<u>264,282,233</u>	<u>246,854,008</u>	<u>215,052,629</u>
<b>Net assets, end of year</b>	<u><u>\$291,762,418</u></u>	<u><u>\$264,282,233</u></u>	<u><u>\$246,854,008</u></u>

**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

As graphically portrayed below, the increase of 18% in interest income-loans is related to the growth in the Agency's portfolio.

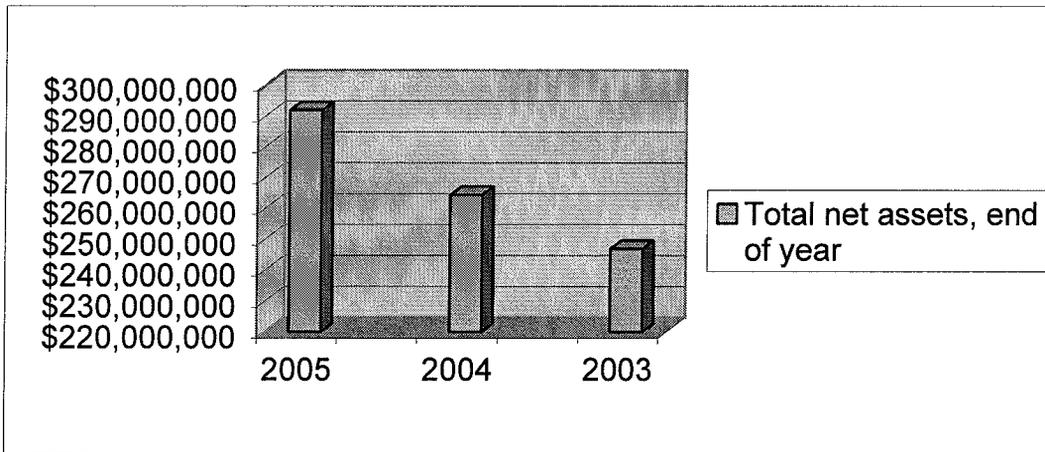
**INVESTMENT INCOME – LOANS AND INVESTMENTS**



As graphically shown above and discussed earlier, investment income increased from \$5,168,533 at June 30, 2004 to \$9,447,001 at June 30, 2005.

The increase in investment income combined with the increase in grant income – federal and state resulted in a 39% increase in total income. Total net assets at June 30, 2005 was \$291,762,418 which was an increase of 10% over the fiscal year ended June 30, 2004.

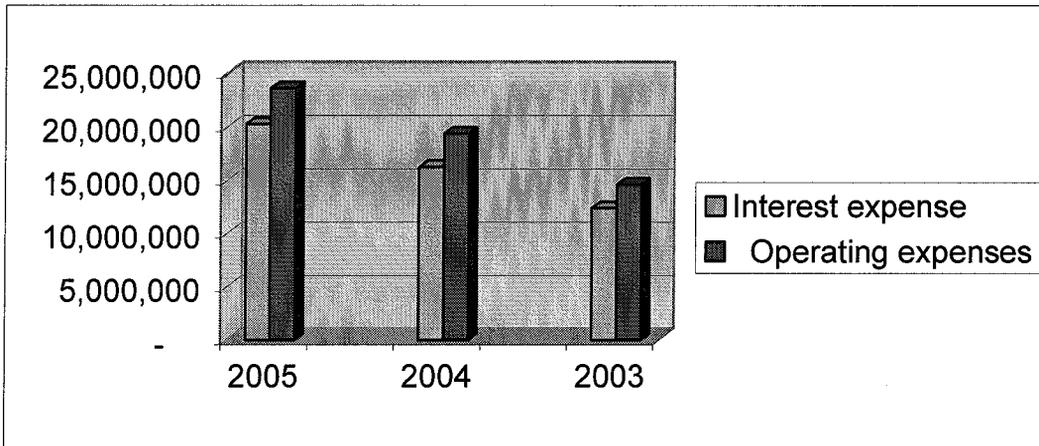
**TOTAL NET ASSETS, END OF YEAR**



**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

An increase of 25% in interest expense is related to the significant growth in the Agency's outstanding bonded indebtedness. As the Agency's outstanding debt increases, operating expenses will increase due to the additional administrative costs associated with overseeing its outstanding bonds and servicing its growing loan portfolio.

**INTEREST EXPENSE AND OPERATING EXPENSES**



**BUDGETARY RESULTS:**

The Agency prepares an annual operating budget (approved by the Agency's Board of Directors) that is used as a management tool for tracking the various revenues and expenses. For the fiscal year ended June 30, 2005 the Agency realized a positive budgetary variance related to its administrative expenses.

**DEBT ADMINISTRATION:**

The Agency administers the Water Pollution Control and the Rhode Island Water Pollution Control revolving loan funds created under Title VI of the Federal Clean Water Act and its State counterpart which is known as the Clean Water State Revolving Fund (CWSRF). The Agency also administers the Drinking Water State Revolving Fund (DWSRF) created under the Federal Safe Drinking Water Act amendments of 1996. The Agency has established a Community Septic System Loan Program (CSSLP) as part of the Federal Clean Water State Revolving Fund. The Agency also provides conduit loans to municipalities for various water and wastewater system improvements. In addition, the Agency created a Rhode Island Zero Interest Loan Fund (RIZILF). This fund was established under the authority of Chapter 55 of the 2000 Public Laws of Rhode Island. The Agency received state bond proceeds totaling \$60,000,000 in fiscal year 2001, of which approximately \$57,000,000 was used to fund the RIZILF and \$3,000,000 was used to provide state match dollars for the Drinking Water State Revolving Fund (DWSRF) program.

At June 30, 2005, the Agency had \$504,660,000 of bond indebtedness, an increase of 23% from the \$411,725,000 outstanding at June 30, 2004. Detailed information related to its Agency's debt is presented in Note 2 to the bonds statement.

**Rhode Island Clean Water Finance Agency  
Management's Discussion and Analysis**

The Agency (Board of Directors and Staff) is proud of the confidence placed in the Agency by the three nationally recognized rating services who continue to rate Agency Bonds as follows:

Fitch - IBCA	AAA
Standard & Poor's	AAA
Moody's	Aaa

The Agency has experienced growth in all aspects of its operations and the future of the Agency continues in a positive direction.

The Agency's Board of Directors voted to designate all net assets in excess of the Agency's annual operating budget to be used for interim and short-term loans to qualified borrowers.

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**STATEMENTS OF NET ASSETS  
JUNE 30, 2005 AND 2004**

	2005	2004
<b><u>ASSETS</u></b>		
<b>Current assets:</b>		
Cash, cash equivalents and investments:		
<b>Unrestricted:</b>		
Cash .....	\$ 34,575,971	\$ 24,484,040
Cash equivalents .....	16,916,810	11,278,927
Investments .....	96,454,410	95,693,982
<b>Total unrestricted cash, cash equivalents and investments</b> .....	<b>147,947,191</b>	<b>131,456,949</b>
<b>Restricted:</b>		
Cash .....	1,259,622	125,421
Investments .....	126,832,370	102,339,998
<b>Total restricted cash, cash equivalents and investments</b> .....	<b>128,091,992</b>	<b>102,465,419</b>
Loans receivable, net .....	21,813,997	19,012,633
Accrued interest receivable:		
Loans .....	4,043,588	3,377,788
Investments .....	2,626,299	1,899,785
Accounts receivable – service fees .....	766,572	581,980
Prepaid expenses and other receivables .....	135,257	77,095
<b>Total current assets</b> .....	<b>305,424,896</b>	<b>258,871,649</b>
<b>Noncurrent assets:</b>		
Loans receivable, net .....	517,280,073	437,224,497
Bond issuance costs, net of accumulated amortization .....	5,144,330	4,153,013
<b>Total noncurrent assets</b> .....	<b>522,424,403</b>	<b>441,377,510</b>
<b>Capital assets:</b>		
Property and equipment, net of accumulated depreciation .....	50,356	57,762
<b>TOTAL ASSETS</b> .....	<b>\$827,899,655</b>	<b>\$700,306,921</b>
<b><u>LIABILITIES</u></b>		
<b>Current liabilities:</b>		
Bonds payable .....	\$ 17,890,000	\$ 11,885,000
Accrued interest payable .....	6,032,955	5,144,271
Accounts payable and accrued expenses .....	4,221,047	2,275,620
<b>Total current liabilities</b> .....	<b>28,144,002</b>	<b>19,304,891</b>
<b>Noncurrent liabilities:</b>		
Bonds payable, net of current portion .....	499,552,197	408,153,869
Bond anticipation note .....	7,719,000	7,719,000
Accrued arbitrage rebate .....	722,038	846,928
<b>Total noncurrent liabilities</b> .....	<b>507,993,235</b>	<b>416,719,797</b>
<b>TOTAL LIABILITIES</b> .....	<b>536,137,237</b>	<b>436,024,688</b>
<b><u>NET ASSETS</u></b>		
Invested in capital assets, net of related debt .....	50,356	57,762
Restricted .....	279,998,423	255,615,508
Unrestricted .....	11,713,639	8,608,963
<b>TOTAL NET ASSETS</b> .....	<b>\$291,762,418</b>	<b>\$264,282,233</b>

SEE ACCOMPANYING NOTES TO THE FINANCIAL STATEMENTS.

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**STATEMENTS OF REVENUES, EXPENSES AND  
CHANGES IN NET ASSETS  
YEARS ENDED JUNE 30, 2005 AND 2004**

	<u>2005</u>	<u>2004</u>
<b>Operating revenues:</b>		
Investment income.....	\$ 9,447,001	\$ 5,168,533
Interest income - loans.....	12,635,671	10,681,840
Grant income - operating .....	2,349,948	2,272,236
Service fees .....	2,148,916	1,746,654
Direct loan fees and other.....	132,047	174,425
Loan origination fees.....	384,524	318,179
<b>Total operating revenues</b> .....	<u>27,098,107</u>	<u>20,361,867</u>
<b>Operating expenses:</b>		
Interest expense .....	20,265,522	16,244,743
Consulting fees - D.E.M and D.O.H. ....	2,349,948	2,272,236
Employee expense.....	395,474	355,109
Finance expense.....	2,593	3,556
Insurance expenses.....	31,158	32,087
Legal fees .....	30,278	61,627
Office expense.....	87,619	77,028
Accounting, auditing, and arbitrage fees.....	26,655	25,927
Depreciation and amortization expense.....	272,314	209,746
Bank fees.....	79,915	63,258
Promotional expenses .....	10,358	7,597
Financial advisor fees .....	34,500	0
Dues and subscriptions.....	4,416	5,149
Seminars.....	1,455	2,085
Business and travel expense .....	7,734	6,033
Miscellaneous expense.....	3,336	1,872
<b>Total operating expenses</b> .....	<u>23,603,275</u>	<u>19,368,053</u>
Operating income.....	3,494,832	993,814
<b>Nonoperating revenue:</b>		
Grant income - non-operating .....	<u>23,985,353</u>	<u>16,434,411</u>
Changes in net assets .....	27,480,185	17,428,225
<b>Net assets, beginning of the year</b> .....	<u>264,282,233</u>	<u>246,854,008</u>
<b>Net assets, end of the year</b> .....	<u>\$291,762,418</u>	<u>\$264,282,233</u>

SEE ACCOMPANYING NOTES TO THE FINANCIAL STATEMENTS.

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**STATEMENTS OF CASH FLOWS  
YEARS ENDED JUNE 30, 2005 AND 2004**

	<u>2005</u>	<u>2004</u>
<b>Cash flows from operating activities:</b>		
Cash receipts for operating grants .....	\$ 2,349,948	\$ 2,272,236
Cash receipts for loan origination fees .....	1,192,499	1,215,681
Cash receipts for service fees .....	1,964,324	1,609,195
Cash receipts for direct loan fees and other .....	132,047	174,425
Cash payments to suppliers .....	(782,700)	(2,869,422)
Cash payments to employees .....	(395,474)	(355,109)
<b>Net cash provided by operating activities .....</b>	<b>4,460,644</b>	<b>2,047,006</b>
<b>Cash flows from capital and related financing activities:</b>		
Purchases of property and equipment .....	(8,944)	(21,669)
<b>Cash flows from non-capital financing activities:</b>		
Proceeds from bond issuance .....	117,696,438	140,912,544
Repayment of bond principal .....	(19,650,000)	(10,350,000)
Non-operating grants received .....	23,985,353	16,434,411
Interest paid on revenue bonds .....	(20,011,853)	(14,927,547)
Bond issuance costs capitalized .....	(1,255,375)	(1,677,486)
Proceeds from bond anticipation note .....	0	7,719,000
<b>Net cash provided by non-capital financing activities .....</b>	<b>100,764,563</b>	<b>138,110,922</b>
<b>Cash flows from investing activities:</b>		
Cash disbursed in lending activities, net .....	(83,664,916)	(121,006,261)
Investment income .....	8,595,597	4,448,514
Interest income – loan program .....	11,969,871	9,997,217
Purchase of investments .....	(114,365,520)	(118,901,678)
Proceeds from sale of investments .....	89,112,720	75,684,689
<b>Net cash used for investing activities .....</b>	<b>(88,352,248)</b>	<b>(149,777,519)</b>
<b>Net increase (decrease) in cash and cash equivalents .....</b>	<b>16,864,015</b>	<b>(9,641,260)</b>
<b>Cash and cash equivalents, beginning of the year .....</b>	<b>35,888,388</b>	<b>45,529,648</b>
<b>Cash and cash equivalents, end of the year .....</b>	<b>\$ 52,752,403</b>	<b>\$ 35,888,388</b>
<b>Reconciliation of operating income to net cash provided by operating activities:</b>		
Operating income .....	\$ 3,494,832	\$ 993,814
Adjustments:		
Investment income .....	(9,322,111)	(4,936,246)
Interest income - loans .....	(12,635,671)	(10,681,840)
Interest expense .....	20,265,522	16,244,743
Depreciation/amortization .....	272,314	209,746
(Increase) decrease in prepaid expenses .....	(58,162)	15,384
Increase (decrease) in accounts payable and accrued expenses .....	1,945,427	(326,351)
Decrease in accrued arbitrage rebate .....	(124,890)	(232,287)
Increase in accounts receivable – service fees .....	(184,592)	(137,459)
Increase in deferred loan origination fees .....	807,975	897,502
<b>Net cash provided by operating activities .....</b>	<b>\$ 4,460,644</b>	<b>\$ 2,047,006</b>

SEE ACCOMPANYING NOTES TO THE FINANCIAL STATEMENTS.

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**(a) Business Purpose and General Information**

The Rhode Island Clean Water Finance Agency (Agency) was established by the State of Rhode Island Legislature as a body politic and corporate and public instrumentality of the State having distinct legal existence separate from the State and does not constitute a department of the State Government. The Agency was established for the express purpose of providing financial assistance in the form of loans to municipalities, sewer commissions and wastewater management districts in Rhode Island for the construction or upgrading of water pollution abatement projects. The Agency will be funded through Federal and State capitalization grants and is authorized to issue revenue bonds to finance the operation and administration of two state revolving fund loan programs.

The Agency commenced operations on July 29, 1990 and began lending activities during the first quarter of fiscal year 1992.

The Agency is a component unit of the State of Rhode Island for financial reporting purposes and as such, the financial statements of the Agency will be included in the State of Rhode Island's Comprehensive Annual Financial Report. The Agency is not subject to Federal or State income taxes.

The Agency adopted the provisions of Governmental Accounting Standards Board Statement No. 34, "Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments." Statement No. 34 established standards for external financial reporting for all state and local governmental entities, which includes a statement of net assets, a statement of activities and changes in net assets, and a statement of cash flows. It requires the classification of net assets into three components – invested in capital assets, net of related debt; restricted; and unrestricted. These classifications are defined as follows:

- *Invested in capital assets, net of related debt* – This component of net assets consists of capital assets, including restricted capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds are not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.
- *Restricted* – This component of net assets consists of constraints placed on net asset use through external constraints imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation. The Agency's net assets are restricted by debt covenants and grantor restrictions.
- *Unrestricted net assets* – This component of net assets consists of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt."

**(b) Basis of Accounting**

The financial statements of the Agency have been prepared on the accrual basis.

The Agency has elected not to apply Financial Accounting Standards Boards statements and interpretations, accounting principles, board opinions, and Accounting Research Bulletins of the Committee of Accounting Procedures issued after November 30, 1989.

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(c) Fund Accounting**

In order to ensure observation of limitations and restrictions placed on the use of resources available to the Agency, the accounts of the Agency will be maintained in accordance with the principles of "Fund Accounting". This is a procedure by which resources for various purposes are classified for accounting and reporting purposes into funds that are in accordance with activities or objectives specified. Separate accounts are maintained for each fund; however, funds will be combined for the presentation of the Agency's financial position and results of operations.

There are currently four separate funds included in the accompanying financial statements:

Water Pollution Control Revolving Fund (WPCRF) – accounts for activity relating to the administering of the Federal Title VI SRF Loan Program (also known as the Clean Water SRF Program).

Rhode Island Water Pollution Control Revolving Fund (RIWPCRF) – accounts for activity relating to the administering of the State SRF Loan Program.

Operating Fund – accounts for the operating activities of the Agency as well as for servicing loans for the Clean Water SRF, the Drinking Water SRF, and the Drinking Water SRF Set-Aside Programs.

Drinking Water State Revolving Fund (DWSRF) – accounts for activity relating to the administering of the Drinking Water SRF Loan Program.

**(d) Investment Income**

Interest earned on investments is recognized as income in the fund in which the investments are held.

**(e) Investments**

The Agency's investments as of June 30, 2005 and 2004 consisted of Treasury obligations, U.S. guaranteed securities in the form of Repurchase Agreements and Guaranteed Investment Contracts (both restricted and unrestricted yields by the Indenture of Trust dated February 15, 1992 and subsequent amendments, between the trustee and the Agency). The Municipal Bond Investors Assurance Corporation and AMBAC has imposed restrictions on indentured funds as to the types of investments the Agency can purchase. These include obligations of the United States government or certain Agencies thereof, guaranteed investment contracts, repurchase agreements, certificates of deposit, money market funds, commercial paper, and notes or bonds of any State meeting specific rating requirements.

Guaranteed Investment Contract providers (GIC providers) are limited to financial institutions rated at least AA, Aa2 and AA from Standard & Poor's, Moody's and Fitch, respectively, or the equivalent for financial strength rating or claims paying ability. The GIC provider must meet the following ratings from S&P, Moody's and Fitch: domestic banks rated at least "AA/Aa2/AA"; US branches of foreign banks rated at least "AA/Aa2/AA" or "AA/Aa2/AA"; insurance companies (or corporations whose obligations are guaranteed by an insurance company (in the form of an insurance policy) or by an insurance holding company) rated "AAA/Aaa/AAA". The provider must be acceptable to the Issuer, MBIA and Ambac.

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(e) Investments (Continued)**

Should the GIC Provider's rating be suspended, withdrawn or downgraded below AA- Fitch, Aa3 by Moody's or AA – by S&P during the term of the Agreement, the Provider must notify the Trustee and, within fifteen (15) days of receipt of notice from the Trustee: (i) provide to the Trustee, or other mutually agreed upon third party custodian, collateral which will be valued and held such that the Provider maintains the applicable minimum rating for the duration and purpose of this Investment, or (ii) at the request of the Trustee, assign the Agreement to an eligible substitute provider, or (iii) at the request of the Trustee, repay the amount on deposit, plus accrued interest to the Trustee.

In accordance with Section 35-10.1-7 of the General Laws of the State of Rhode Island, dealing with the collateralization of public deposits, all time deposits with maturities of greater than 60 days and all deposits in institutions that do not meet its minimum capital standards as required by its Federal regulator must be collateralized. The Agency did not have any deposits in fiscal year 2005 and 2004 which required collateralization based on the aforementioned criteria.

GASB Statement No. 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools," was implemented during 1998. Fair values are established by quoted market values. Unrealized gains and losses from the changes in fair value are recognized as investment income.

**(f) Cash and Cash Equivalents**

Cash equivalents include repurchase agreements with maturities of three months or less when purchased.

The Agency's cash management program includes the automatic "sweeping" of the Agency's bank accounts into overnight collateralized repurchase agreements. The Agency had repurchase agreements of \$16,916,810 and \$11,278,927 at June 30, 2005 and 2004, respectively.

**(g) Property and Equipment**

Property and equipment are stated at cost. Depreciation is calculated on the straight-line basis over the estimated useful lives of the assets. Depreciation expense for fiscal years 2005 and 2004 totaled \$16,350 and \$17,021, respectively. The Agency's capitalization threshold is any individual item with a total cost greater than \$500.

Depreciation is provided by use of the straight-line method over the following estimated useful lives of the assets:

<u>Asset Category</u>	<u>Estimated Useful Life</u>
Computer equipment	3 years
Equipment, furniture, and fixtures	3 – 5 years
Leasehold improvements	7 – 20 years

**(h) Accrued Arbitrage Rebate**

Investment income is limited to the bond yield on certain tax-exempt bond issues. Interest income in excess of this limit has been reserved for rebate in accordance with applicable financing documents. Investment income earned in excess of the allowable amounts will be remitted to the Federal Government as required by the applicable laws and regulations.

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

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**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(i) Loan Related Fees and Costs**

Loan fees and certain direct loan origination costs are deferred, and the net fee is recognized in income using the effective yield method over the contractual life of the loans. The Agency had unamortized deferred loan origination fees totaling \$4,956,921 and \$4,148,945 at June 30, 2005 and 2004, respectively.

**(j) Bond Issuance Costs**

Costs relating to bond issuance consist of professional fees and staff expenses and are capitalized and amortized on a straight-line basis over the life of the bond or to the date at which the Agency has the right to redeem the bond, whichever is less. Amortization expense for fiscal years 2005 and 2004 totaled \$255,965 and \$192,725, respectively.

**(k) Bond Premium**

Bond premiums are amortized using the effective interest method over the respective lives of the serial bonds. Amortization of bond premiums, which are charged against interest expense, totaled \$572,734 and \$276,913 for fiscal years 2005 and 2004, respectively.

**(l) Allowance for Loan Losses**

Management reviews loan receivable balances on a periodic basis for possible uncollectible amounts. In the event management determines a specific need for an allowance, provision for loss will then be provided. Should a borrower default on a loan, the remedy is found in the loan agreement which is backed by the full taxing power of the borrowing municipality in the form of a general obligation pledge or in the full revenue collecting ability of the Agency's revenue borrowers. Further, the Indenture of Trust as it relates to the Local Interest Subsidy Trust (LIST) serves as a debt service reserve fund. Based upon prior years' experience and management's evaluation of outstanding loan receivable balances, no allowance for loan losses has been provided at June 30, 2005 and 2004.

**(m) Grant Revenue**

The Agency recognizes state and federal grant revenues upon the acceptance of their request for drawdown of these revenues by the grantor agency.

**(n) Use of Estimates**

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

**(o) Operating Revenues and Expenses**

Operating revenues and expenses of the Agency consist of revenues earned and expenses incurred relating to the operation of the Agency. All other revenues and expenses are reported as nonoperating revenue and expenses.

**(p) Restricted Assets**

Restricted assets of the Agency represent monies designated for debt service reserve and to subsidize borrower interest rates.

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**(q) Recently Issued Accounting Standards**

The Agency has implemented GASB No. 40, Deposits and Investment Risk Disclosures, for the year ended June 30, 2005, which changes the way the Agency presents the details of its cash and investment disclosures. The adoption of this Statement did not have a significant impact on the Agency's financial position or results of operations.

The Agency will adopt the following new accounting pronouncements in future years:

- √ GASB Statement No. 42 - Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries, effective for the Agency's fiscal year ending June 30, 2006.
- √ GASB Statement No. 45 - Accounting and Financial Reporting by Employers for Post-employment Benefits Other Than Pensions, effective for the Agency's fiscal year ending June 30, 2008.

The impact of these pronouncements on the Agency's financial statements has not been determined.

**(r) Income Tax**

The Agency is exempt from federal and state income taxes.

**2. BONDS PAYABLE**

Since its inception, the Agency has issued revenue bonds to local governments to finance water pollution abatement projects. The bonds are special obligations of the Agency payable solely from and secured by the particular funds, assets or revenues, generated by the Borrower Bonds. The Bonds do not constitute an indebtedness of the State or any of its subdivisions and none of its revenues are pledged. The Agency has no taxing power.

The Agency has the following revenue bonds outstanding at June 30:

	<u>2005</u>	<u>2004</u>
<b>Water Pollution Control Revolving Fund Revenue Bonds:</b>		
1992 Series A Bonds, dated February 15, 1992, with serial bonds of \$15,875,000 at rates varying from 3.5% to 6.6% due annually from October 1, 1993 through October 1, 2008 and term bonds of \$2,390,000 at 6.7% due October 1, 2010 and \$2,650,000 at 6.75% due October 1, 2013. On February 4, 1999, the Agency advance refunded \$9,210,000 of the outstanding bonds.....	\$ 1,120,000	\$ 1,355,000

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**2. BONDS PAYABLE (Continued)**

	<u>2005</u>	<u>2004</u>
<b>Water Pollution Control Revolving Fund Revenue Bonds (Continued):</b>		
1993 Series A Bonds, dated February 15, 1993, with serial bonds of \$23,450,000 at rates varying from 3.8% to 9.2% due annually from October 1, 1996 through October 1, 2010 and a term bond of \$10,185,000 at 5.4% due October 1, 2015 .....	21,010,000	22,665,000
1994 Series A Bonds, dated June 1, 1994, with serial bonds of \$18,495,000 at rates varying from 5.0% to 7.7% due annually from October 1, 1995 through October 1, 2012 and a term bond of \$3,935,000 at 5.875% due October 1, 2015. On February 4, 1999, the Agency advance refunded \$5,725,000 of the outstanding bonds ....	7,910,000	8,985,000
1995 Series A Bonds, dated December 15, 1995, at rates varying from 4.15% to 7.00% due annually from October 1, 1997 through October 1, 2016.....	3,930,000	4,255,000
1999 Series A Bonds, dated January 1, 1999, with serial bonds of \$19,590,000 at rates varying from 3.7% to 5.25% due annually from October 1, 2002 through October 1, 2016 and term bonds of \$3,765,000 at 4.75% due October 1, 2018 and \$2,470,000 at 4.75% due October 1, 2020.....	24,970,000	25,260,000
1999 Series C Bonds, dated August 1, 1999, with serial bonds of \$24,010,000 at rates varying from 4.15% to 5.50% due annually from October 1, 2001 through October 1, 2019 .....	20,325,000	21,480,000
2000 Series A Bonds, dated December 1, 2000 with serial bonds of 26,550,000 at rates varying from 4.50% to 5.125% due annually from October 1, 2001 through October 2020 .....	22,080,000	23,205,000
2002 Series A Bonds, dated April 1, 2002, with serial bonds of \$29,305,000 at rates varying from 3.00% to 5.50% due annually from October 1, 2002 through October 1, 2022 .....	26,890,000	28,045,000
2002 Series B Bonds, dated October 1, 2002, with serial bonds of \$76,035,000 at rates varying from 2.0% to 5.0% due annually from October 1, 2004 through October 1, 2022 .....	70,650,000	73,960,000
2003 Series A Bonds, dated May 22, 2004, with serial bonds of \$14,870,000 at rates varying from 1.220% to 4.280% due annually from October 1, 2005 through October 1, 2023 .....	14,870,000	14,870,000
2003 Series B Bonds, dated November 13, 2004, with serial bonds of \$67,965,000 at rates varying from 2.00% to 5.250% due annually from October 1, 2005 through October 1, 2024 .....	67,965,000	67,965,000
2004 Series A Bonds, dated December 30, 2004, with serial bonds of \$69,625,000 at rates varying from 2.50% to 5.00% due annually from October 1, 2005 through October 1, 2025 .....	69,625,000	0

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**2. BONDS PAYABLE (Continued)**

	<u>2005</u>	<u>2004</u>
<b>Safe Drinking Water Revenue Bonds (Continued):</b>		
1994 Market Rate Series A Bonds, dated December 1, 1994, with serial bonds of \$6,765,000 at rates varying from 5.1% to 6.5% due annually from January 1, 1996 through January 1, 2009 and a term bond of \$5,235,000 at 6.7% due January 1, 2015. This bond was currently refunded during March, 2005 .....	0	8,310,000
2003 Series A Bonds, dated December 17, 2003, with term bonds of \$5,840,000 at 5.00% due annually from October 1, 2025 through October 1, 2028 and term bonds of \$13,500,000 at 5.00% due annually from October 1, 2029 through October 1, 2035.....	19,340,000	19,340,000
2003 Series B bonds (federally taxable), dated December 17, 2003, with term bonds of \$7,655,000 at 6.00% due annually from October 1, 2025 through October 1, 2035 .....	7,655,000	7,655,000
2004 Series A Bonds, dated March 11, 2004, with serial bonds of \$40,170,000 at rates varying from 2.00% to 5.00% due annually from October 1, 2005 through October 1, 2024 .....	40,170,000	40,170,000
2005 Series A Bonds, dated March 23, 2005, with serial bonds of \$42,960,000 at rates varying from 3.00% to 5.00% due annually from October 1, 2006 through October 1, 2027 .....	42,960,000	0
<b>Wastewater Treatment System Revenue Bonds:</b>		
1997 Series Bonds, dated August 1, 1997. The Series 1997 Bonds mature on September 1, 2022, with sinking fund payments due on September 1, 1999, and September 1, 2018 through September 1, 2022, inclusive. Interest of 5.8% is due annually on March 1, and September 1.....	28,490,000	28,490,000
<b>Refunding Bonds:</b>		
1999 Series B Bonds, dated January 1, 1999 with serial bonds of 16,830,000 at rates varying from 3.0% to 4.75% due annually from October 1, 1999 through October 1, 2015 .....	14,700,000	15,715,000
Subtotal .....	504,660,000	411,725,000
Less: amount deferred on refunding .....	(1,104,616)	(987,243)
Add: bond premium (discount) net of amortization .....	13,886,813	9,301,112
<b>Total bonds payable .....</b>	<b><u>\$517,442,197</u></b>	<b><u>\$420,038,869</u></b>

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**2. BONDS PAYABLE (Continued)**

The following schedule reflects the changes in bonds payable:

	<u>June 30, 2005</u>	<u>June 30, 2004</u>
<b>Balance at beginning of the year</b> .....	\$411,725,000	\$286,945,000
Additions.....	112,585,000	135,130,000
Retirements.....	<u>(19,650,000)</u>	<u>(10,350,000)</u>
<b>Balance at end of the year</b> .....	<b><u>\$504,660,000</u></b>	<b><u>\$411,725,000</u></b>

Annual principal and interest requirements are as follows for the years ending June 30:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006 .....	\$ 17,890,000	\$ 22,895,807	\$ 40,785,807
2007 .....	20,835,000	22,214,398	43,049,398
2008 .....	22,455,000	21,443,709	43,898,709
2009 .....	23,655,000	20,547,376	44,202,376
2010 .....	24,130,000	19,593,891	43,723,891
2011 - 2015 .....	124,145,000	82,365,810	206,510,810
2016 - 2020 .....	127,445,000	53,244,420	180,689,420
2021 - 2025 .....	110,225,000	20,110,561	130,335,561
2026 - 2030 .....	17,235,000	6,250,974	23,485,974
2031 - 2035 .....	13,490,000	2,694,150	16,184,150
2036 .....	3,155,000	83,500	3,238,500
<b>Total</b> .....	<b><u>\$504,660,000</u></b>	<b><u>\$271,444,595</u></b>	<b><u>\$776,104,595</u></b>

***Advanced Refunding of Debt***

On February 4, 1999, the Agency issued the 1999 Series B Subordinated Refunding Bonds. The proceeds from this issue were used to defease portions of the 1992 and 1994 Series A Bonds. The Agency established an irrevocable escrow trust fund pursuant to a Refunding Trust Agreement between the Agency and US Bank Corporate Trust Services. The escrow fund is irrevocably pledged solely for the repayment of principal, redemption premium, if any, and interest on the aforementioned refunded bonds. Under the escrow agreement, the refunded bonds will be called for redemption at each series first applicable optional redemption date. As those bonds have, in effect, been redeemed under the defeasance, they are no longer outstanding under the Agency's Basic Bond Resolution and, therefore, they are not entitled to the pledge of the Basic Bond Resolution. Accordingly, these bonds and the related escrow funds are not reflected in these financial statements as of June 30, 2005 and 2004.

The following represents the refunded bonds and principal amount refunded:

<u>Series</u>	<u>Refunding Date</u>	<u>Principal Amount Refunded</u>	<u>Defeased Bonds Outstanding June 30, 2005</u>
1992	February 4, 1999.....	\$ 9,210,000	\$ -0-
1994 A	February 4, 1999.....	<u>5,725,000</u>	<u>5,665,000</u>
	<b>Total</b> .....	<b><u>\$14,935,000</u></b>	<b><u>\$5,665,000</u></b>

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

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**2. BONDS PAYABLE (Continued)**

***Advanced Refunding of Debt (Continued)***

The difference between the net carrying amount of the refunded bonds and the amount placed in escrow was \$1,469,895. This amount has been deferred and is being amortized over the shorter of the remaining life of the refunding bonds or the life of the 1994 Series A Bonds. The amount deferred on refunding is shown in the financial statements as a reduction of bonds payable and is being charged to operations through the fiscal year ending June 30, 2016 using the straight-line method, since use of the effective interest method is not deemed to be materially different. Amortization totaling \$87,755 was recorded in fiscal year 2005 and 2004. The Agency completed the advance refunding to reduce its total debt service payments over the next 17 years by \$1,351,567 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of approximately \$956,000.

***Current Refunding***

During fiscal year 2005, the Agency refunded its 1994 Series A bonds dated December 1, 1994 with an outstanding balance of \$7,765,000. The difference between the amount required to repay the previously issued debt (reacquisition price) and the net carrying amount of the old debt was \$210,388. This amount has been deferred and is being amortized over the shorter remaining life of the refunded bonds (120 months). The amount deferred on refunding is reported in the financial statements as a reduction of bonds payable and is being charged to operations through fiscal year ending 2015 using the straight-line method, since use of the effective interest method is not deemed to be materially different. Amortization totaling \$5,260 was recorded in fiscal year 2005. The Agency completed the current refunding to reduce its debt service payments over the next ten years by \$1,564,216 and to obtain an economic gain (difference between the present values of the old and new debt service payments) of approximately \$1,213,000.

***Bond Anticipation Note***

On March 9, 2004, the Agency issued a 2004 Series A Bond Anticipation Note on behalf of a local community to provide interim financing. The Note principal is \$7,719,000, matures on March 1, 2007, and requires interest at 2.60%.

**3. LOANS RECEIVABLE**

At June 30, 2005 and 2004, the Agency had loans receivable of \$544,050,991 and \$460,386,075 representing 94 and 83 outstanding loans, respectively. At June 30, 2005 and 2004, the current portion of loans receivable (net of loan origination fees) totaled \$21,813,997 and \$19,012,633, respectively. In addition, at June 30, 2005 and 2004, the Agency had outstanding unused commitments totaling approximately \$118,129,964 and \$108,307,870 for the disbursement of future loans. For financial reporting purposes on the statement of net assets, total 2005 outstanding loans receivable of \$544,050,991 have been reduced by unamortized loan origination fees totaling \$4,956,921. For 2004, total outstanding loans receivable of \$460,386,075 have been reduced by unamortized loan origination fees totaling \$4,148,945.

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

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**3. LOANS RECEIVABLE (Continued)**

The borrowers are obligated to repay the full balance of loan agreements; however, funds are disbursed by the Agency in accordance with the loan agreements as costs are incurred for the projects for which the loans are intended. The Agency disburses funds to the borrowers and/or vendors, no more than once a month, after receipt of an official request for disbursement, which is accompanied by supporting documentation. The Agency is obligated to disburse funds only up to the value of the loan agreement, and is not responsible for any excess costs incurred by the borrower. The borrower, in turn, is obligated to make principal and interest payments in accordance with the repayment schedules per the loan documentation even if funds have not been fully disbursed by the Agency at the time of first payment. Loans are usually repaid over 20 years with either level principal or level total payments. The balances of the loan agreements may include financing for the interest expense to be incurred by the borrowers during the period of construction.

The Agency has established a Local Interest Subsidy Trust (LIST) Fund, which is restricted by the Indenture of Trust between the trustee and the Agency and may be used to make the required bond payments in the event of default by the borrowers.

At June 30, 2005, the Agency had outstanding loans receivable to three borrowers representing 70% of the Agency's total loan receivable balance. At June 30, 2004, the Agency had outstanding loans receivable to two borrowers representing 61% of the Agency's total loan receivable balance.

**4. CASH, CASH EQUIVALENTS, INVESTMENTS AND RESTRICTED (LIST INVESTMENTS)**

**(a) Cash**

Custodial Credit Risk, Deposits - The Agency does not have a deposit policy for custodial credit risk.

At June 30, 2005, the carrying amount of the Agency's cash balance was \$35,835,595. The bank balance was \$35,960,495 as of the same period. Of the bank balance at June 30, 2005, \$100,000 was covered by the Federal Depository Insurance Corporation (the "FDIC"), and \$35,860,495 (\$35,735,495 was held in money market trust accounts), which are currently uninsured.

At June 30, 2004, the carrying amount of the Agency's cash balance was \$24,609,461. The bank balance was \$24,914,687 as of the same period. Of the bank balance at June 30, 2004, \$100,000 was covered by the Federal Depository Insurance Corporation (the "FDIC"), and \$24,814,687 (\$19,739,687 was held in money market trust accounts), which were uninsured.

**(b) Cash Equivalents, and Other Investments**

The table below categorizes the Agency's investments so as to provide an indication of the level of market risk and credit risk assumed by the Agency at year end. Market risk is the risk that the market value of an investment, collateral securing the investment or securities underlying a repurchase agreement will decline. Credit risk can be associated with the issuer of a security, with a financial institution holding deposits, or with the custodian of securities or collateral. Category 1 includes insured or registered securities held by the Agency or its agent in the Agency's name. Category 2 includes uninsured and unregistered, with securities held by the counterparty's trust department or agent in the Agency's name. Category 3 includes uninsured and unregistered with securities held by the counterparty or by its trust department or agent, but not in the Agency's name. The Agency does not have any investments within Category 3, and therefore is not subject to the custodial credit risk disclosures of GASB 40.

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**4. CASH, CASH EQUIVALENTS, INVESTMENTS AND RESTRICTED (LIST INVESTMENTS (Continued))**

**(b) Cash Equivalents, and Other Investments (Continued)**

At June 30, 2005, the investments held by the Agency were as follows:

<u>Description</u>	<u>Category</u>			<u>Fair Value</u>
	<u>1</u>	<u>2</u>	<u>3</u>	
<b>Cash Equivalents:</b>				
Collateralized Repurchase Agreements...	\$16,916,810	\$ 0	\$-0-	\$ 16,916,810
<b>Other Investments:</b>				
Federal National Mortgage Association ...		13,889,000		13,889,000
Collateralized Repurchase Agreements...	<u>26,249,579</u>			26,249,579
Subtotal .....	<u>\$43,166,389</u>	<u>\$13,889,000</u>	<u>\$-0-</u>	
<b>Other Investments not subject to categorization:</b>				
Collateralized Investment Contracts.....				39,659,143
Uncollateralized Investment Contracts.....				<u>143,489,058</u>
Subtotal .....				<u>223,286,780</u>
<b>Total other investments.....</b>				<u>\$240,203,590</u>

The following investment contracts represented more than 5% of the Agency's total investments at June 30, 2005:

	<u>Amount</u>	<u>Maturity Date</u>	<u>Interest Rate</u>
<b>Collateralized Investment Contracts:</b>			
AIG Matched Funding Corp.....	\$ 12,927,372	2022	4.75%
MBIA, Inc.....	17,254,871	2015 - 2020	5.47 - 7.48%
<b>Uncollateralized Investment Contracts:</b>			
Bayerische Landesbank.....	17,219,543	2016	5.33 - 5.60%
AIG Matched Funding Corp.....	21,212,983	2023 - 2025	3.57 - 4.18%
XL Asset Funding, LLC .....	26,967,631	2008	3.67%
Citigroup Financial Products, Inc.....	40,413,385	2005 - 2006	1.26 - 2.68%
FSA Capital Management Services, LLC.	37,675,529	2024 - 2027	4.67 - 4.79%

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**4. CASH, CASH EQUIVALENTS, INVESTMENTS AND RESTRICTED (LIST INVESTMENTS (Continued))**

**(b) Cash Equivalents, and Other Investments (Continued)**

At June 30, 2004, the investments held by the Agency were as follows:

<u>Description</u>	<u>Category</u>			<u>Fair Value</u>
	<u>1</u>	<u>2</u>	<u>3</u>	
<b>Cash Equivalents:</b>				
Collateralized Repurchase Agreements...	\$11,278,927	\$ 0	\$-0-	\$11,278,927
<b>Other Investments:</b>				
Federal National Mortgage Association ...		13,056,000		13,056,000
Collateralized Repurchase Agreements...	42,336,783			42,336,783
Subtotal .....	<u>\$53,615,710</u>	<u>\$13,056,000</u>	<u>\$-0-</u>	
<b>Other Investments not subject to categorization:</b>				
Collateralized Investment Contracts.....				54,460,667
Uncollateralized Investment Contracts.....				88,180,530
Subtotal .....				<u>198,033,980</u>
<b>Total other investments.....</b>				<u>\$209,312,907</u>

The following investment contracts represented more than 5% of the Agency's total investments at June 30, 2004:

	<u>Amount</u>	<u>Maturity Date</u>	<u>Interest Rate</u>
<b>Collateralized Repurchase Agreements:</b>			
Westdeutsche Landesbank.....	\$ 12,000,000	2019	6.280%
Morgan Stanley Flexible Agreements .....	25,378,681	2006	1.412%
<b>Collateralized Investment Contracts:</b>			
AIG Matched Funding Corp.....	13,116,644	2022	4.750%
MBIA, Inc.....	31,139,023	2004 - 2020	1.433 - 7.480%
<b>Uncollateralized Investment Contracts:</b>			
Bayerische Landesbank.....	17,448,992	2016	5.33 - 5.60%
AIG Matched Funding Corp.....	25,157,612	2005 - 2023	1.13 - 4.184%
Citigroup Financial Products, Inc.....	32,809,928	2005	1.260%
FSA Capital Management Services, LLC.	12,764,000	2024	4.71%

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**5. CAPITALIZATION GRANTS**

**(a) Clean Water State Revolving Fund (CWSRF):**

The Agency receives capitalization grants from the Environmental Protection Agency for the Clean Water State Revolving Fund under Title VI of the Clean Water Act. These grants are used to fund the Agency's lending activities and to reimburse the State Department of Environmental Management for up to 4% of the capitalization grant for expenses incurred for services they provide the Agency related to these lending activities. In order to obtain the federal monies under the Title VI grant program, the Agency must also obtain a commitment for state matching funds of 20% of the federal award.

The following is a table of the federal and state matching funds awarded to the Agency and the balances remaining for drawdown under Title VI of the Clean Water Act as of June 30, 2005:

<u>Grant Year</u>	<u>Award</u>	<u>Balance Remaining for Drawdown</u>
1995:		
Federal award .....	\$ 8,254,100	\$ 0
State match .....	1,650,820	0
1996:		
Federal award .....	13,547,500	467,943
State match .....	2,709,500	0
1997:		
Federal award.....	4,127,100	165,084
State match .....	825,420	0
2001:		
Federal award .....	8,921,900	629,408
State match .....	1,784,380	0
2003:		
Federal award .....	8,883,300	150,560
State match .....	1,776,660	0
2004:		
Federal award .....	8,888,700	2,014,704
State match .....	1,777,740	0
2005:		
Federal award (applied for August 2005).....	7,208,600	7,208,600
State match (applied for August 2005).....	1,441,720	1,441,720

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**5. CAPITALIZATION GRANTS (Continued)**

**(b) Drinking Water State Revolving Fund (DWSRF)**

The Agency also receives capitalization grants from the Environmental Protection Agency for the Drinking Water State Revolving Fund under Section 1452 of the Safe Drinking Water Act Amendments of 1996. The grants will be used to provide loans to water suppliers for system improvements and to provide funding for various improvement programs administered by the RI Department of Health to bring water suppliers in the State up to the minimum standards promulgated by the Safe Drinking Water Act. As in the Clean Water SRF, up to 4% is to be used for program administration by both the Agency and Department of Health. In order to receive the funding from E.P.A., the Agency must commit 20% of the Federal award in the form of State matching funds. The Agency agrees to provide, through methods available to it, the appropriate state matching funds to each grant.

The following table shows the DWSRF federal awards and remaining balances as of June 30, 2005:

<u>Grant Year</u>	<u>Award</u>	<u>Balance Remaining for Drawdown</u>
1997:		
Federal award .....	\$12,558,800	\$ 777,813
State match .....	2,511,760	0
1998:		
Federal award .....	7,121,300	654,505
State match .....	1,424,260	0
1999:		
Federal award .....	7,463,800	1,255,764
State match .....	1,492,760	0
2000:		
Federal award .....	7,757,000	301,890
State match .....	1,551,400	0
2001:		
Federal award .....	7,789,100	3,730,505
State match .....	1,557,820	0
2002:		
Federal award .....	8,052,500	7,132,353
State match .....	1,610,500	0
2003:		
Federal award .....	8,004,100	8,004,100
State match .....	1,600,820	1,600,820
2004:		
Federal award .....	8,303,100	8,303,100
State match .....	1,660,620	1,660,620

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

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**6. DEFERRED COMPENSATION**

The Agency offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The plan, available to all Agency employees, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

The Agency implemented the Governmental Accounting Standards Board, Statement No. 32, *Accounting and Financial Reporting for Internal Revenue Code Section 457 Deferred Compensation Plans*. All assets and income of the plan are held in trust for the exclusive benefit of the participants and their beneficiaries. As a result, deferred compensation investments and the respective liability have been removed from the Agency's financial statements for the years ended June 30, 2005 and 2004.

The Agency is obligated to remit to the administrator an amount equal to 5% of employee compensation on a monthly basis. The Agency's contribution totaled \$15,430 and \$14,147 for the years ended June 30, 2005 and 2004, respectively. Employees are allowed to make contributions to the plan up to, but not exceeding, the lesser of 33 1/3% of their individual compensation or \$14,000 (\$18,000 if age 50 or older) for 2005. There is no additional obligation incurred by the Agency as a result of the employee contributions. The Agency has an obligation to prudently manage these monies.

**7. OPERATING LEASE**

On June 1, 1998, the Agency entered into a seven-year lease for the rental of its corporate offices. During fiscal year 2005, the Agency incurred rent expense of \$49,840, consisting of rent expense of \$48,528 plus \$1,312 in additional property tax assessments. During fiscal year 2004, the Agency incurred rent expense of \$49,181, consisting of scheduled lease payments of \$47,260, plus \$1,921 in additional property tax assessments. On April 10, 2003, the Agency amended its existing lease agreement due to the expansion of its facilities. The new lease is for a period of 60 months commencing June 1, 2003 and expires May 2008.

The following schedule summarizes the Agency's required future minimum lease payments:

<u>Year Ending June 30:</u>	<u>Amount</u>
2006 .....	\$ 49,744
2007 .....	49,744
2008 .....	<u>45,599</u>
<b>Total</b> .....	<b><u>\$145,087</u></b>

(CONTINUED)

**RHODE ISLAND CLEAN WATER FINANCE AGENCY**

**NOTES TO FINANCIAL STATEMENTS  
JUNE 30, 2005 AND 2004**

**8. PROPERTY AND EQUIPMENT**

The summary of changes in property and equipment at June 30, 2005 are summarized below:

	<u>Balance at June 30, 2004</u>	<u>Additions</u>	<u>Retirements</u>	<u>Balance at June 30, 2005</u>
<b>Cost:</b>				
Computers .....	\$ 45,554	\$ 8,944		\$ 54,498
Furniture and fixtures .....	20,406			20,406
Equipment.....	15,424			15,424
Leasehold Improvements .....	29,701			29,701
<b>Total cost</b> .....	<u>111,085</u>	<u>8,944</u>	<u>0</u>	<u>120,029</u>
<b>Accumulated depreciation:</b>				
Computers .....	34,958	8,611		43,569
Furniture and fixtures .....	7,010	3,342		10,352
Equipment.....	10,612	2,912		13,524
Leasehold Improvements .....	743	1,485		2,228
<b>Total accumulated depreciation</b> .....	<u>53,323</u>	<u>16,350</u>	<u>0</u>	<u>69,673</u>
<b>Net capital assets</b> .....	<u>\$ 57,762</u>	<u>\$ (7,406)</u>	<u>\$0</u>	<u>\$ 50,356</u>

**9. COMMITMENTS AND CONTINGENCIES**

**Capitalization Grants**

The Rhode Island Clean Water Finance Agency receives grants from the Environmental Protection Agency (EPA) and the State of Rhode Island to fund its loan program activities. The activities of these programs through June 30, 2005, were subject to an audit under the Single Audit Act of 1996 by our independent auditors. In addition to being audited in accordance with the Single Audit Act of 1996, oversight agencies require periodic compliance audits by the grantors or their representatives. The Environmental Protection Agency conducts annual fiscal and regulatory compliance reviews to determine that Agency activities are in compliance with EPA regulations. As of June 30, 2005, no expenditures of the Agency have been disallowed. Agency officials believe that any future disallowance of expenditures would not be material.

**10. DESIGNATION OF UNRESTRICTED NET ASSETS**

The Agency's Board has designated its unrestricted net assets as follows:

**Operating Fund - Interim/Short-term Loan Program**

On October 4, 2004, the Board voted to designate all net assets in excess of the Agency's annual operating budget to be used for interim and short-term loans to qualified borrowers.

**11. RISK MANAGEMENT**

The Agency is exposed to various risks of loss related to tort; theft of, damage to, and destruction of assets; errors or omissions and injuries to employees. As a result, the Agency has purchased commercial insurance to protect itself from potential liabilities from losses or claims. To date, the Agency has not incurred any claims or losses.

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