

**AUDIT REPORT
OF THE
NEBRASKA DEPARTMENT OF
ENVIRONMENTAL QUALITY
CLEAN WATER
STATE REVOLVING FUND PROGRAM
JULY 1, 2001 THROUGH JUNE 30, 2002**

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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

BACKGROUND

The Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program (Program) was established pursuant to Title VI of the Federal Clean Water Act, as amended by the Water Quality Act of 1987. Neb. Rev. Stat. Sections 81-15,147 created the Wastewater Treatment Facilities Construction Assistance Act. The Federal Water Quality Act and State statutes established the Clean Water State Revolving Fund Program to provide loans, at reduced interest rates, to finance the construction of publicly owned water pollution control facilities, non-point source pollution control projects, and estuary management plans. Instead of making grants to communities that pay for a portion of the building of wastewater treatment facilities, the Program provides for low interest loans to finance the entire cost of qualified projects. The Program provides a flexible financing source which can be used for a variety of projects. Loans made by the Program must be repaid within 20 years, and all repayments, including interest and principal, must remain in the Program.

The Program was capitalized by the United States Environmental Protection Agency (EPA) by a series of grants starting in 1989. States are required to provide an additional 20 percent of the Federal capitalization grant as matching funds in order to receive a Federal grant. As of June 30, 2002, the EPA had awarded over \$100 million in capitalization grants to the State. The award of this \$100 million required the State to contribute \$20 million in matching funds. The State provided appropriations to contribute \$.955 million of the funds to meet the State's matching requirement. Additional matching funds were obtained through the issuance of revenue bonds.

The Program is administered by the Nebraska Department of Environmental Quality (Department). The Department's primary activities with regard to the Program include the making of loans for water pollution control facilities and the management and coordination of the Program. The Nebraska Environmental Quality Council approves the rules and regulations of the Department and the Program's Intended Use Plan.

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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY CLEAN WATER STATE REVOLVING FUND PROGRAM

INDEPENDENT AUDITORS' REPORT

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We have audited the accompanying financial statements of the business-type activities of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program (Program), as of and for the year ended June 30, 2002, as listed in the Table of Contents. These financial statements are the responsibility of the Program's management. 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 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 our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program, are intended to present the financial position, and the changes in financial position and cash flows, of only that portion of the business-type activities of the State that is attributable to the transactions of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program. They do not purport to, and do not, present fairly the financial position of the State of Nebraska as of June 30, 2002, and the changes in its financial position and its cash flows for the year then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program, as of June 30, 2002, and the respective changes in financial position and cash flows thereof for the year 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 March 5, 2003, on our consideration of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

In accordance with the *U.S. Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*, we have also issued our report dated March 5, 2003, on our consideration of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program's compliance with certain provisions of laws, regulations, and grants.

March 5, 2003

Pat Reding, CPA
Assistant Deputy Auditor

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
 CLEAN WATER STATE REVOLVING FUND PROGRAM
BALANCE SHEET
 June 30, 2002

	<u>Enterprise Fund</u>
ASSETS:	
CURRENT ASSETS:	
Cash in State Treasury (Note 2)	\$ 33,592,544
Loans Receivable - Current (Note 3)	7,349,413
TOTAL CURRENT ASSETS	40,941,957
NONCURRENT ASSETS:	
Loans Receivable (Note 3)	80,126,542
TOTAL NONCURRENT ASSETS	80,126,542
TOTAL ASSETS	\$ 121,068,499
LIABILITIES:	
CURRENT LIABILITIES:	
Accounts Payable	\$ 454
TOTAL CURRENT LIABILITIES	454
NET ASSETS:	
Unrestricted	121,068,045
TOTAL NET ASSETS (Note 5)	121,068,045
TOTAL LIABILITIES AND NET ASSETS	\$ 121,068,499

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
 CLEAN WATER STATE REVOLVING FUND PROGRAM
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN FUND NET ASSETS
 For the Fiscal Year Ended June 30, 2002

	Enterprise Fund
OPERATING REVENUES:	
Loan Fees Administration (Note 6)	\$ 772,040
Bonds Issued	2,180,000
Interest on Loans	2,831,213
Interest on Fund Balance Trustee	26,476
Interest on Fund Balance (Note 7)	1,558,827
TOTAL OPERATING REVENUES	7,368,556
OPERATING EXPENSES:	
Administrative Costs	506,729
Small Town Grants (Note 8)	155,864
Principal Payments on Bonds	2,180,000
Interest Expense - State Match Bonds	29,637
Cost of Bond Issuance	52,872
TOTAL OPERATING EXPENSES	2,925,102
OPERATING INCOME	4,443,454
CAPITAL CONTRIBUTIONS - FEDERAL GRANTS	12,163,828
CHANGE IN NET ASSETS	16,607,282
TOTAL NET ASSETS, BEGINNING OF YEAR	104,460,763
TOTAL NET ASSETS, END OF YEAR	\$ 121,068,045

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM
STATEMENT OF CASH FLOWS
For the Fiscal Year Ended June 30, 2002

	Enterprise Fund
CASH FLOWS FROM OPERATING ACTIVITIES:	
Receipts from Customers	\$ 8,539,537
Interest on Investments	1,585,303
Payments to Borrowers	(17,933,321)
Payments to Employees and Vendors	(507,515)
Small Town Grants	(155,864)
Cost of Bond Issuance	(52,872)
Bond Principal Payments	(2,180,000)
Bonds Issued	2,180,000
Bond Interest Payments	(29,637)
NET CASH PROVIDED BY OPERATING ACTIVITIES	(8,554,369)
CASH FLOWS FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES:	
Funds Received from Environmental Protection Agency	12,163,828
NET CASH FROM NONCAPITAL AND RELATED FINANCING ACTIVITIES	12,163,828
NET INCREASE IN CASH AND CASH EQUIVALENTS	3,609,459
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	29,983,085
CASH AND CASH EQUIVALENTS, END OF YEAR	\$ 33,592,544
RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:	
Operating Income	\$ 4,443,454
ADJUSTMENTS TO RECONCILE OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:	
(Increase) in Loans Receivable	(12,997,037)
(Decrease) in Accounts Payable	(786)
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ (8,554,369)

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

For the Fiscal Year Ended June 30, 2002

1. Summary of Significant Accounting Policies

- A. **Basis of Presentation.** The accompanying financial statements of the Nebraska Department of Environmental Quality (Department) - Clean Water State Revolving Fund Program (Program) have been prepared in conformance with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

The financial statements have been prepared primarily from accounts maintained by the State Accounting Administrator of the Department of Administrative Services.

- B. **Reporting Entity.** The Clean Water State Revolving Fund Program is a program within the Department and is established under and governed by the Clean Water Act of the Federal Government and by laws of the State of Nebraska. The Department is a State agency established under and governed by the laws of the State of Nebraska. As such, the Department is exempt from State and federal income taxes. The Program's management has also considered all potential component units of the Program for which it is financially accountable, and other organizations which are fiscally dependent on the Program's management, or the significance of their relationship with the Program's management are such that exclusion would be misleading or incomplete. GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the Department to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the Department.

As required by generally accepted accounting principles, these financial statements present the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program. No component units were identified. The Program is part of the primary government for the State of Nebraska's reporting entity.

- C. **Fund Structure.** The Program's accounts are maintained in accordance with the principles of fund accounting to ensure compliance with limitations and restrictions placed on the use of resources available to it. Under fund accounting, individual funds are established for the purpose of carrying on activities or attaining objectives in accordance with specific regulations, restrictions, or limitations. Each individual fund is a self-balancing set of accounts recording

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. Summary of Significant Accounting Policies (Continued)

cash and other financial resources, together with liabilities and residual equities or balances, and changes therein. The Program is made up of four funds on the State of Nebraska Accounting System. It includes the following funds as identified in the Wastewater Treatment Facilities Construction Assistance Act:

- Clean Water Facilities Fund – General Fund 1000, Federal Fund 4841, and Trust Fund 6847
- Construction Administration Fund – Cash Fund 2846.

These funds are used to account for revenues and expenses for loans and administrative expenses of the Program.

The activity of these four State of Nebraska funds have been combined and reported as an enterprise fund, which under governmental GAAP is a proprietary fund type. This fund type reflects transactions used to account for those operations that are financed and operated in a manner similar to a private business. The accounting for the Program's transactions in this manner is a requirement of the Environmental Protection Agency (EPA) as they and the Department have decided that the determination of revenues earned, expenses incurred, and/or net income is necessary to demonstrate the success of the Program and to assure the EPA that the Program will be available in perpetuity as intended.

- D. Basis of Accounting.** The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. An enterprise fund is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of the fund are included on the balance sheet. Enterprise fund operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets.

Enterprise funds utilize the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

In reporting the financial activity of its enterprise fund, the Program's management applied all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinion, and Accounting Research Bulletins of the Committee on Accounting Procedures.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. **Summary of Significant Accounting Policies (Concluded)**

E. **Cash and Cash Equivalents.** Cash in State Treasury is maintained in a short term investment pool and is considered cash equivalents.

F. **Loans Receivables.** The State operates the Program as a direct loan program, whereby loans are made to communities. The entire Clean Water Program is funded, on the average, 83.33% from federal capitalization grants and 16.67% from State matching funds. Loan funds are disbursed to the local agencies as they expend funds for the purposes of the loan. Interest is calculated from the date that funds are advanced, and after the final disbursement has been made, the payment schedule identified in the loan agreement is adjusted for the actual amounts disbursed, and accrued interest during the project period. The interest rates on loans range from 3% to 4% and the terms are between 10 to 20 years. The current loans receivable amount was determined using the amount of principal payment due to the Program at June 30, 2002, which was collectible in fiscal year 2003.

No provisions were made for uncollectible accounts as all loans were current, and management believed all loans would be repaid according to the loan terms. There was a provision for the Program to intercept State aid to a community in default of its loan.

G. **Accounts Payable.** Due to limitations of the State of Nebraska Accounting System a cutoff must be made on July 31st of each year when determining the amount of accounts payable that exists for the current year. Any information that would change this figure will be disregarded and shown as an expense of the year the payment is made and not when the liability is incurred.

2. **Cash in State Treasury**

Cash in State Treasury as reported on the balance sheet is under the control of the State Treasurer or other administrative bodies as determined by law. All cash deposited with the State Treasurer is maintained in a short-term investment pool. The State Investment Officer invests the deposited cash in short-term securities and other investments. All interest revenue is allocated to the general fund except allocations required by law to be made to other funds. All funds of the Clean Water State Revolving Fund Program were designated for investment during fiscal year 2002. Amounts are allocated on a monthly basis based on average balances of all invested funds.

3. **Loans Receivable**

As of June 30, 2002, the Program had made loans to 77 communities that totaled more than \$87 million. The outstanding balances of the largest ten loans, which represent approximately 55 percent of the total loans, were as follows:

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
 CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

3. Loans Receivable (Concluded)

City	Outstanding Balance
Aurora	\$ 2,908,685
Cozad	2,888,515
Fremont	3,082,515
Gretna	4,725,822
Kearney	5,433,925
Lincoln	5,592,566
Norfolk	7,453,840
Omaha	5,740,682
Sarpy County SID	4,758,974
Scottsbluff	5,375,262
Total	\$ 47,960,786

4. Bonds Payable

The defeasance of the 1994 and 1998 Revenue bonds occurred on May 3, 2000. There were no revenue bonds outstanding in the Program as of June 30, 2002.

In 2000, the Nebraska Investment Finance Authority (NIFA) issued \$5,150,000 of defeasance revenue bonds, dated May 3, 2000, to defease outstanding 1994 and 1998 series revenue bonds. In conjunction with the defeasance, the 1994 series bonds maturing on or after July 1, 2002 were called for redemption on July 1, 2002 at a price of \$2,189,835 (101%). The 1998 series bonds maturing on or after July 1, 2006 are scheduled to be called for redemption on July 1, 2006 at a price of \$1,350,975 (100%). As a result, the 1994 and 1998 series bonds are considered defeased and the liability for these bonds has been removed from the Balance Sheet. At June 30, 2002, \$2,105,000 of the 1994 series bonds and \$2,020,000 of the 1998 series bonds remained to be paid from the investments held by the Trustee.

On May 3, 2000, NIFA deposited \$5,097,231 with the Trustee (Wells Fargo Bank, Iowa) to defease the 1994 and 1998 series bonds. The 2000 Series Defeasance Revenue Bonds matured on May 3, 2000. Therefore, at June 30, 2002, no 2000 series bonds were outstanding.

The Environmental Protection Agency (EPA) requires the Program issue revenue bonds to provide the State's matching funds. During the fiscal year, the Program issued and redeemed \$2,180,000 in short-term revenue bonds. Therefore, at June 30, 2002, no revenue bonds were outstanding. Bonds payable at June 30, 2002 are as follows:

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

4. Bonds Payable (Concluded)

	Beginning Balance	Additions	Retirement	Ending Balance
Bonds Payable	\$ -	\$ 2,180,000	\$ 2,180,000	\$ -

5. Net Assets

Included in the Net Assets is the total amount of capitalization grants drawn from the EPA by the Department. The following summarizes the capitalization grants awarded, drawn, and the remaining balance as of June 30, 2002.

Year	Grant Amount	Amount Drawn	Balance
1989	\$ 4,773,100	\$ 4,773,100	\$ -
1990	4,964,560	4,964,560	-
1991	10,821,580	10,821,580	-
1992	9,938,500	9,938,500	-
1993	9,830,300	9,830,300	-
1994	6,061,600	6,061,600	-
1995	6,263,600	6,263,600	-
1996	10,319,661	10,319,661	-
1997	3,119,900	3,119,900	-
1998	7,019,996	7,019,996	-
1999	6,857,600	6,857,600	-
2000	6,834,000	6,834,000	-
2001	6,797,400	6,797,400	-
2002	6,855,000	2,692,913	4,162,087
Totals	\$ 100,456,797	\$ 96,294,710	\$ 4,162,087

The following is a summary of changes in the total contributed capital.

Contributed Capital July 1, 2001	\$ 85,085,822
Contributed During the Year Funds - Received From EPA	12,163,828
Contributed Capital June 30, 2002	\$ 97,249,650

Also included in the Contributed Capital is a total of all general funds received by the Program from the Legislature of the State of Nebraska. These assets were to be used as match for the Program for the initial capitalization grant received by the State. The State contributed \$300,000 and \$655,000 in fiscal years ended June 30, 1989 and 1990, respectively.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

6. Loan Fees Administration

The reported amount comes from a fee charged to loan recipients each year based on the amount of the loan outstanding. The fee ranged from .5% to 1% per annum and was collected semi-annually. Of the total collected, \$274,200 was used as match for the capitalization grant.

7. Interest on Fund Balance Held by State Treasurer

The reported amount represents the earnings the Program has received from idle funds invested by the Treasurer of the State of Nebraska. Interest is credited on approximately the twenty-fifth day of each subsequent month.

8. Small Town Grants

Small Town Grants are made to communities that have a population of 800 people or less. The total maximum of Small Town Grants awarded in any one fiscal year is \$500,000. The maximum a community can receive is \$100,000 concurrent with a Program loan. The Loan Fees Administration is used to fund these grants.

9. Operating Revenues and Expenses

Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Program's principal ongoing operations. The principal operating revenue of the Program is the Loan Fees Administration. Interest revenues are also operating revenues since making loans is the primary purpose of the Program. The principal operating expenses of the Program are administration expenses and loan forgiveness. Interest expenses are also operating expenses since making loans is the primary purpose of the Program.

10. State Employees' Retirement Plan (Plan)

The Plan is a single-employer defined contribution plan administered by the Public Employees Retirement Board in accordance with the provisions of the State Employees Retirement Act and may be amended through Legislative action. In the defined contribution plan, retirement benefits depend on total contributions, investment earnings, and the investment options selected. Prior to April 18, 2002 membership in the Plan was required of all permanent full-time employees on reaching the age of thirty and completion of twenty-four months of continuous service and voluntary participation was permitted for all permanent full-time or part-time employees upon reaching age twenty and twelve months of service within a five-year period. Any individual appointed by the Governor may elect not to become a member of the Plan. Legislative Bill 687 (2002), effective April 18, 2002, stated all permanent full-time employees shall begin participation in the Plan upon completion of twelve continuous months of service.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

10. **State Employees' Retirement Plan (Plan) (Concluded)**

Employees contribute 4.33% of their monthly compensation until such time as they have paid during any calendar year a total of eight hundred sixty four dollars, after which time they shall pay a sum equal to 4.8% of their monthly compensation for the remainder of such calendar year. The Department matches the employee's contribution at a rate of 156% of the employee's contribution.

The employee's account is fully vested. The employer's account is vested 100% after five years participation in the plan (prior to April 18, 2002) or at retirement. Legislative Bill 687 (2002), effective April 18, 2002, changed the vesting requirement to a total of three years of participation in the system, which includes the twelve-month eligibility period or credit for participation in another governmental plan prior to actual contribution to the Plan.

For the fiscal year ended June 30, 2002, the Clean Water State Revolving Fund Program's employees contributed \$12,825 and the Department contributed \$20,007 for these employees.

11. **Contingencies and Commitments**

Risk Management. The Department is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; natural disasters; and health care insurance. The Department, as part of the primary government for the State, participates in the State's risk management program. The Nebraska Department of Administrative Services (DAS) Division of Risk Management is responsible for maintaining the insurance and self-insurance programs for the State. The State has chosen not to purchase insurance except for:

1. Motor vehicle liability which is insured for the first \$5 million of exposure per accident. Insurance is also purchased for medical payments, physical damage, and uninsured and underinsured motorists with various limits and deductibles.
2. Health care insurance for employees selecting certain coverage options. All health care insurance was purchased.
3. Employee dishonesty which is bonded for the first \$1 million annually with a \$10,000 retention per incident.
4. Real and personal property on a blanket basis for net loss in excess of \$200,000 per loss occurrence, with a limit of \$250,000,000 per loss occurrence. Newly acquired properties are only covered up to \$1,000,000 for 60 days or until the value of the property is reported to the insurance company. The perils of flood and earthquake are covered up to \$10,000,000.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

11. Contingencies and Commitments (Concluded)

No settlements exceeded commercial insurance coverage in any of the past three fiscal years. Health care insurance is funded in the Risk Management Internal Service Fund through a combination of employee and State contributions. Workers compensation is also funded in the Risk Management Internal Service Fund through assessments on each agency based on total agency payroll and past experience. Tort claims, theft of, damage to, and destruction of assets; errors and omissions; and natural disasters would be funded through the State General Fund or by individual agency assessments as directed by the Legislature, unless covered by purchased insurance. No amounts for estimated claims have been reported in the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund's financial statements.

12. GASB 34

In June 1999, GASB issued Statement No. 34, Basic Financial Statements – and Management Discussion and Analysis – for State and Local Governments. The State of Nebraska implemented the Statement for the fiscal year ended June 30, 2002.

The Department implemented GASB 34 by presenting its financial statements in a format as required by GASB 34. However, as explained in Note 1.D. the Program's financial statements are presented on the accrual basis of accounting. Previous period financial statements of the Program were also prepared on the accrual basis of accounting; therefore, these financial statements, even though in different format, are comparable to previous period financial statements of the Program.

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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY CLEAN WATER STATE REVOLVING FUND PROGRAM REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

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We have audited the financial statements of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program as of and for the year ended June 30, 2002, and have issued our report thereon dated March 5, 2003. The report was modified to emphasize the financial statements present only the funds of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program. 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.

Compliance

As part of obtaining reasonable assurance about whether the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial

statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program in a separate letter dated March 5, 2003.

This report is intended solely for the information and use of the Program, the appropriate Federal and regulatory agencies, and citizens of the State of Nebraska, and is not intended to be and should not be used by anyone other than these specified parties.

March 5, 2003

Pat Reding, CPA
Assistant Deputy Auditor

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**REPORT ON COMPLIANCE
WITH REQUIREMENTS APPLICABLE TO THE
NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY
CLEAN WATER STATE REVOLVING FUND PROGRAM
IN ACCORDANCE WITH U.S. ENVIRONMENTAL PROTECTION
AGENCY AUDIT GUIDE FOR CLEAN WATER AND DRINKING
WATER STATE REVOLVING FUND PROGRAMS**

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We have audited the compliance of the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program with the types of compliance requirements described in the *U.S. Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs* that were applicable for the year ended June 30, 2002. We audited the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program’s compliance with requirements governing: Allowability for Specific Activities, Allowable Costs/Costs Principles, Cash Management, State Matching, Period of Availability of Funds and Binding Commitments, Program Income, Reporting, Subrecipient Monitoring, and Special Tests and Provisions.

Compliance with these requirements is the responsibility of the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program’s management. Our responsibility is to express an opinion on the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program’s compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the *U.S. Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on the Program occurred. An audit includes

examining, on a test basis, evidence about the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program’s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program’s compliance with those requirements.

As identified below and in a separate letter to the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program’s management dated March 5, 2003, the Department did not comply with the following requirements.

- The Department has not filed their annual financial status report with the United States Environmental Protection Agency (EPA) for the federal fiscal year ending September 30, 2002. This report was due December 31, 2002.
- The Department did not file their annual report with the EPA for the State fiscal year ending June 30, 2002 in a timely manner. The report was due September 30, 2002, but was not filed until February 2003.
- The Department has not filed their quarterly federal cash report since January 2002. The reports were due within 15 days following the end of each quarter.

In our opinion, except for the reporting noncompliance issues described in the preceding paragraph, the Nebraska Department of Environmental Quality – Clean Water State Revolving Fund Program complied, in all material respects, with the requirements referred to above that are applicable to the Program for the fiscal year ended June 30, 2002.

This report is intended solely for the information and use of the Program, the federal awarding agencies, and citizens of the State of Nebraska, and is not intended to be and should not be used by anyone other than these specified parties.

March 5, 2003

Pat Reding, CPA
Assistant Deputy Auditor