



A REPORT
TO THE
MONTANA
LEGISLATURE

LEGISLATIVE AUDIT
DIVISION

09-25

FINANCIAL AUDIT

Montana Water Pollution Control and Drinking Water State Revolving Fund Programs

*Department of
Environmental Quality*

*Department of Natural
Resources and Conservation*

*For the fiscal year ended
June 30, 2008*

FEBRUARY 2009

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FINANCIAL AUDITS

Financial audits are conducted by the Legislative Audit Division to determine if the financial statements included in this report are presented fairly and the agency has complied with laws and regulations having a direct and material effect on the financial statements. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States Government Accountability Office. Financial audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

The Single Audit Act Amendments of 1996 and OMB Circular A-133 require the auditor to issue certain financial, internal control, and compliance reports in addition to those required by Government Auditing Standards. This individual agency audit report is not intended to comply with these requirements. The Legislative Audit Division issues a statewide biennial Single Audit Report which complies with the above reporting requirements. The Single Audit Report for the two fiscal years ended June 30, 2007, was issued January 23, 2008. The Single Audit Report for the two fiscal years ended June 30, 2009, will be issued by March 31, 2010. Copies of the Single Audit Report can be obtained by contacting:

Single Audit Coordinator
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Room 277, State Capitol
P.O. Box 200802
Helena, MT 59620-0802

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LEGISLATIVE AUDIT DIVISION

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel



Deputy Legislative Auditors
James Gillett
Angie Grove

February 2009

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the fiscal year 2007-08 financial audit of the Montana Water Pollution Control State Revolving Fund (WPCSRF) and Drinking Water State Revolving Fund (DWSRF) Programs. The Department of Natural Resources and Conservation requested the audit of these programs because annual audits are required by the federal Environmental Protection Agency. These programs are administered jointly by the Department of Natural Resources and Conservation and the Department of Environmental Quality.

The objectives of a financial audit include determining if the programs' financial statements fairly present the programs' financial position at June 30, 2008, and the results of operations for the fiscal year then ended. We tested compliance with state and federal laws that have a direct and material impact on the financial statements.

The WPCSRF program provides loans at a reduced interest rate to finance construction of publicly owned water pollution control facilities, nonpoint source pollution control projects, and estuary management plans. Water pollution control loans are comprised of federal grants and state match funds and may be financed up to 30 years. As of June 30, 2008, the WPCSRF had \$144,511,963 of outstanding loans, including advances to other funds.

The DWSRF program provides low interest loans to communities for the construction of drinking water treatment facilities. Drinking water loans are comprised of federal grants and state match funds and may be financed up to 30 years. At June 30, 2008, the DWSRF had \$89,969,216 of outstanding loans, including advances to other funds.

On page A-1, you will find the Independent Auditor's Report followed by the financial statements and accompanying notes. We issued an unqualified opinion which means the reader can rely on the information presented. The programs' financial statements begin on page A-3. Our opinion on the programs' supplementary financial information is on page B-1. The supplementary information begins on page B-3.

Our Report on internal control over financial reporting and on compliance and other matters based on an audit of financial statements performed in accordance with *Government Auditing Standards* is on page C-1. Auditing standards require us to communicate, in writing, control deficiencies over financial reporting we identified based on an audit of financial statements performed in accordance with

Government Auditing Standards and considered to be significant or material. A control deficiency exists when the design or operation of a control does not allow management or employees to prevent or detect misstatements on a timely basis. A significant deficiency is one or more control deficiencies that affects management's ability to accurately process transactions. A material weakness is one or more significant deficiencies that adversely affect management's ability to fairly present its financial statements.

Table 1 below outlines the material weakness we identified during this audit. As the objective of our audit was to determine the reasonableness of the programs' financial statements, as discussed above, we make no recommendations for corrective action in this report.

Subject	Significant Deficiency	Material Weakness	Page
Ineffective Controls to Ensure the Notes to the Financial Statements are Accurately Compiled.	Yes	Yes	C-1

Auditing standards also required us to communicate, in writing, material noncompliance with the provisions of laws, regulations, contracts, and grant agreements that could have a direct and material effect on the determination of financial statements amounts. Our report on the consideration of internal control over financial reporting and on our tests of compliance with certain provisions of laws, regulations, and grant agreements indicates our tests disclosed no instances of noncompliance or other matters required to be reported.

Officials from both departments have reviewed this report and agree with its contents. The response from the departments is at page D-1. We thank the directors of the Department's of Environmental Quality and Natural Resources and Conservation and their staff for their cooperation and assistance during the audit.

Respectfully submitted,

/s/ Tori Hunthausen

Tori Hunthausen, CPA
Legislative Auditor

APPOINTED AND ADMINISTRATIVE OFFICIALS

**Department of Environmental
Quality**

Richard Opper, Director

Tom Livers, Deputy Director

Dean Rude, Chief Financial Officer, Financial Services

**Department of Natural Resources
and Conservation**

Mary Sexton, Director

Ann Bauchman, Administrator, Centralized Services Division

Anna Miller, Bureau Chief, Loan & Financial
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For additional information concerning the Montana Water
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Monica Huyg, Legal Counsel



Deputy Legislative Auditors
James Gillett
Angie Grove

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the accompanying Combined Balance Sheet, Special Revenue and Debt Service Funds, of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of June 30, 2008, and the related Combined Statement of Revenues, Expenditures, and Changes in Fund Balances, Special Revenue and Debt Service Funds, for the fiscal year then ended. The information contained in these financial statements is the responsibility of the management of the Department of Environmental Quality and the Department of Natural Resources and Conservation. 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 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 audit provides a reasonable basis for our opinion.

As discussed in the notes to the financial statements, the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the state of Montana that is attributable to the transactions of the programs. They do not purport to, and do not, present fairly the financial position of the state of Montana as of June 30, 2008, or the changes in its financial position for the fiscal year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of June 30, 2008, and results of operations for the fiscal 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 January 15, 2009, on our consideration of the programs' 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 results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

January 15, 2009

**MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED BALANCE SHEET
SPECIAL REVENUE AND DEBT SERVICE FUNDS
JUNE 30, 2008**

	WATER POLLUTION CONTROL			DRINKING WATER			(MEMORANDUM ONLY) TOTAL
	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	
ASSETS							
Cash and Cash Equivalents	\$19,083,706	(\$538)	\$2,664,464	\$7,638,302	(\$16,474)	\$1,672,655	\$31,042,115
Interest Receivable	321,036		1,245,651	232,003		912,585	2,711,275
Accounts Receivable	25,766			30,432			56,198
Due from Federal Government		6,253			181,112		187,365
Due from Other Fund/Business Unit	25,153						25,153
Loans Receivable	129,375,594			89,969,216			219,344,810
Advances to Other Funds	15,136,369						15,136,369
Total Assets	\$163,967,624	\$5,715	\$3,910,115	\$97,869,954	\$164,638	\$2,585,240	\$268,503,286
LIABILITIES AND FUND BALANCES							
Liabilities:							
Accounts Payable	\$206,421		\$245	\$169,776	\$98,213		\$474,655
Payroll Payable	11,394	\$5,340		5,220	66,156		88,110
Interest Payable	51,461			72,592		(\$3,096)	120,957
Due to Other BU or Fund				25,153		5,568	30,721
Deferred Revenue		375			269		644
Loans Payable						650,000	650,000
Total Liabilities	\$269,276	\$5,715	\$245	\$272,741	\$164,638	\$652,472	\$1,365,087
Fund Balances							
Reserved for LT Loans/Notes/Advances	\$144,511,963			\$89,969,216			\$234,481,179
Reserved for Debt Service			\$3,909,870			\$1,932,768	5,842,638
Unreserved, Undesignated	19,186,385			7,627,996	\$0		26,814,381
Total Fund Balance	\$163,698,348	\$0	\$3,909,870	\$97,597,212	\$0	\$1,932,768	\$267,138,198
Total Liabilities and Fund Balances	\$163,967,624	\$5,715	\$3,910,115	\$97,869,954	\$164,638	\$2,585,240	\$268,503,286

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

**MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS
COMBINED STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
SPECIAL REVENUE AND DEBT SERVICE FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	WATER POLLUTION CONTROL			DRINKING WATER			(MEMORANDUM ONLY) TOTAL
	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	STATE SPECIAL REVENUE	FEDERAL SPECIAL REVENUE	DEBT SERVICE	
REVENUES:							
Federal Capitalization Grant Revenue		\$4,714,484			\$7,888,901		\$12,603,385
Interest Income on Investments	\$681,478		\$64,413	\$214,342		\$42,535	1,002,768
Investment Appreciation/Gains (Depreciation/Losses)	(342)			4,727		244	4,629
Interest Income from Loans	1,077,058		4,416,955	656,702		2,579,818	8,730,533
Other Income	4			36	189		229
TOTAL REVENUES	\$1,758,198	\$4,714,484	\$4,481,368	\$875,807	\$7,889,090	\$2,622,597	\$22,341,544
EXPENDITURES:							
Program Administration/Set-Asides	\$433,482	\$129,750	\$3,543	\$258,195	\$1,516,278		\$2,341,248
TOTAL EXPENDITURES	\$433,482	\$129,750	\$3,543	\$258,195	\$1,516,278	\$0	\$2,341,248
Excess Revenues Over (Under) Expenditures	\$1,324,716	\$4,584,734	\$4,477,825	\$617,612	\$6,372,812	\$2,622,597	\$20,000,296
OTHER FINANCING SOURCES:							
<i>Operating Transfers In:</i>							
Recycled Transfer from Water Pollution Control				\$2,500,000			\$2,500,000
Debt Service Sweep	\$612,283			584,350			1,196,633
Loan Loss Reserve Sweep	1,463,012			754,644			2,217,656
Bond/RAN/BAN Proceeds	900,000			1,300,000			2,200,000
Federal Capitalization Grants	4,585,106			6,372,812			10,957,918
Investment Earnings from State Special Revenue			\$6,298			\$101,166	107,464
Total Other Financing Sources	\$7,560,401	\$0	\$6,298	\$11,511,806	\$0	\$101,166	\$19,179,671
OTHER FINANCING USES:							
Bond Principal			\$1,870,000			\$690,000	\$2,560,000
Bond Interest			531,285			513,665	1,044,950
Loan Interest			7,924			14,429	22,353
Cost of Issuance	\$11,500			\$12,500			24,000
<i>Operating Transfers Out:</i>							
Debt Service Sweep			612,283			584,350	1,196,633
Loan Loss Reserve Sweep			1,463,012			754,644	2,217,656
Federal Capitalization Grants		\$4,585,106		\$6,372,812			10,957,918
Recycled Transfer to Drinking Water	2,500,000						2,500,000
Bond/RAN/BAN Proceeds			900,000			1,300,000	2,200,000
Investment Earnings to Debt Service	6,298			101,166			107,464
Total Other Financing Uses	\$2,517,798	\$4,585,106	\$5,384,504	\$113,666	\$6,372,812	\$3,857,088	\$22,830,974
Excess (deficiency) of Revenues and Other Financing Sources over (under) Expenditures and Other Financing Uses	\$6,367,319	(\$372)	(\$900,381)	\$12,015,752	\$0	(\$1,133,325)	\$16,348,993
Fund Balances July 1, 2007	\$157,316,581	\$0	\$4,810,251	\$85,581,460	\$0	\$3,096,078	\$250,804,370
Prior Year Adjustments	14,449	372	0	1	0	(29,985)	(15,163)
Fund Balances June 30, 2008	\$163,698,348	\$0	\$3,909,870	\$97,597,212	\$0	\$1,932,768	\$267,138,198

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

**MONTANA STATE WATER POLLUTION CONTROL AND
DRINKING WATER STATE REVOLVING FUND PROGRAMS
SPECIAL REVENUE AND DEBT SERVICE FUND
NOTES TO FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

1. Organization of the Programs

The State of Montana Water Pollution Control State Revolving Fund (WPCSRF) Program was established pursuant to Title VI of the Federal Water Quality Act of 1987. This federal act established the WPCSRF program to replace the construction grants program. It provides a flexible financing source to loan money 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 building wastewater treatment facilities, the WPCSRF provides for low interest rate loans to finance the entire cost of qualified projects or to refinance debt obligations on projects. The State of Montana first incurred expenditures in the WPCSRF Program in state fiscal year (SFY) 1992.

The State of Montana Drinking Water State Revolving Fund (DWSRF) Program was established pursuant to the 1996 Amendments to the Federal Safe Drinking Water Act. This federal act established the DWSRF program for states to make loans to community water systems and non-profit non-community water systems. Instead of making grants to communities that pay for a portion of building drinking water treatment facilities, the DWSRF provides for low interest rate loans to finance the entire cost of qualified projects or to refinance debt obligations on projects that began after July 1, 1993. The State of Montana first incurred expenditures in the DWSRF Program in SFY 1997.

WPCSRF and DWSRF loan agreements allow up to 30 years for repayment. All repayments of interest and principal must remain in the revolving funds. Both programs are capitalized through U.S. Environmental Protection Agency (EPA) grants. States are required to provide 20 percent of the federal capitalization grant as matching funds for DWSRF, and 16.67 percent for WPCSRF, in order to receive a grant. The State of Montana issues General Obligation Bonds, Revenue Anticipation Notes (RANs), and Bond Anticipation Notes (BANs) to provide the required state matching funds. RANs and BANs are funded through INTERCAP Loans from the Montana Department of Commerce.

The programs are jointly administered by the Technical and Financial Assistance Bureau of the Department of Environmental Quality (DEQ) and the Conservation and Resource Development Division of the Department of Natural Resources and Conservation (DNRC). The revolving fund programs do not have any full time employees. Both funds are charged for time spent on SRF activities by department employees. The charges include salaries and benefits of the employees and operating expenses as well as indirect costs.

2. Summary of Significant Accounting Policies

A. State Revolving Fund (SRF) Program Fund Structure

Both programs use Special Revenue and Debt Service funds, as appropriate, to report the financial position and the results of operations. A Special Revenue Fund accounts for the proceeds of specific revenue sources that are restricted to expenditures for specified purposes. A Debt Service Fund accounts for resources accumulated for payment of principal and interest on general long-term obligation debt, BANs and RANs. Montana maintains State Special Revenue and Federal Special Revenue Funds. The SRF program revenues and expenses include transactions from each Special Revenue Fund. Special Revenue and Debt Service Funds are considered governmental funds.

A fund is a separate accounting entity with a self-balancing set of accounts. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions and activities.

B. Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds are accounted for using a current financial resources measurement focus. Current financial resources means that, generally, only assets and current liabilities are included on the balance sheet. Operating statements of governmental funds present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets.

Governmental funds use the modified accrual basis of accounting. The modified accrual basis is the accrual basis adapted to the governmental fund-type measurement focus. Under the modified accrual basis of accounting, revenues are recorded when received in cash unless susceptible to accrual. Revenues are susceptible to accrual if they are measurable and available within sixty days after the end of the fiscal year to finance expenditures of the fiscal year. Revenues are deferred if material and received before the normal time of receipt or if received for a particular activity and the expense for that activity has not been incurred prior to fiscal year-end. Expenditures are recognized when the related fund liability is incurred, with the following exceptions:

- 1) principal and interest on long-term debt are recognized when due;
- 2) prepayments are accounted for as expenditures in the period of acquisition;
- 3) inventory items are considered expenditures when purchased.

The Loans Receivable account resides in the State Special Revenue fund for each program. This account represents the total principal due on the loans outstanding for each program.

C. Prior Period Adjustments

Prior period adjustments reported in the accompanying financial statements relate to corrections of errors or other correcting adjustments from prior periods not otherwise reported as sources or uses of funds.

3. Cash/Cash Equivalents

Cash and cash equivalents consist of funds deposited with the US Bank, N.A. as trustee, and include investments categorized as cash equivalents. Cash equivalents are defined as short-term, highly liquid investments with original maturities of three months or less.

Disclosures Relating to Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. In accordance with the investment policy defined in the bonds trust indenture, the cash equivalent funds invested by US Bank, N.A., as trustee, are held in a Treasury Obligations Money Market Fund that invests exclusively in short-term U.S. Treasury obligations and repurchase agreements secured by U.S. Treasury obligations. The U.S. Treasury obligations in which the fund invests include U.S. Treasury bonds, notes, and bills, and are backed by the full faith and credit of the United States government.

Disclosures Relating to Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party.

The investment policy as defined in the Indenture of Trust, and contract with the trustee, does not require collateralization for cash and securities held by the trustee. Securities are registered with the Federal Reserve Bank under "U.S. Bank as trustee for the State of Montana Department of Natural Resources and Conservation." However, U.S. Bank policy is to collateralize money market funds at 101% of cost.

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The investment policy for the programs, as specified in the Indenture of Trust, does not explicitly address interest rate risk. However, the investment policy implicitly limits interest rate risk for cash equivalents by emphasizing liquidity, holding investments to maturity, and narrowly defining the eligible investments. In general, a shorter average maturity for fixed-income securities held in the money market fund means less sensitivity to interest rate changes. The average maturity in the fund as of June 30, 2008, is nineteen days. The effective duration method result is NA because the program does not have any debt investments at this time.

<u>Investment Type</u>	<u>Book Value</u>	<u>Moody's Rating</u>	<u>Effective Duration</u>
Held by trustee: Money market funds	\$31,056,931	Aaa	NA

4. Investments

Power to Invest and Investment Policy

The Board of Examiners of the State of Montana authorizes the sale and issuance of general obligation bonds, RANs, and BANs to provide the state match for the SRF programs through the issuance of an Indenture of Trust. The Board of Examiners is comprised of the Governor, Attorney General and the Secretary of State for the State of Montana. The Indenture of Trust specifies the eligible investments meeting defined rating and risk criteria in which the state may invest. The state invests funds through its trustee bank, US Bank, N.A.

Eligible investments are limited, generally, to obligations of, or guaranteed as to principal and interest by the United States of America, or by any agency or instrumentality thereof. A primary investment objective is to make investments that mature, or are subject to redemption, on or prior to the date or dates that the department anticipates that money will be required to make payments.

Disclosures Relating to Credit Risk

Generally, credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. The short- and long-term investments made by US Bank, N.A., as trustee, are held in U.S. Treasury bills and notes. U.S. Treasury bills have maturities of one year or less and U.S. Treasury notes have maturities greater than one year from the date of issuance.

Disclosures Relating to Custodial Credit Risk

Custodial credit risk for investments is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The investment policy as defined in the Indenture of Trust, and contract with the trustee, does not require collateralization for cash and securities held by the trustee. Securities are registered with the Federal Reserve Bank under "U.S. Bank as trustee for the State of Montana Department of Natural Resources and Conservation."

Disclosures Relating to Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The investment policy, as specified in the Indenture of Trust, does not explicitly address interest rate risk. However, the investment policy implicitly limits interest rate risk by emphasizing liquidity, holding investments to maturity, and narrowly defining the eligible investments.

5. Loans Receivable

Montana operates both SRF programs as direct loan programs. Loans made to communities through the Water Pollution Control Program are funded 83.33 percent by the federal EPA capitalization grant, and 16.67 percent by the state match amount. Some Water Pollution Control Program loans are made as recycled, or “second round”, loans and are disbursed from loan repayment funds. Loans made by the Drinking Water Program are funded approximately 80 percent by the federal EPA capitalization grant, and 20 percent by the state match amount. The Drinking Water Program makes recycled loans that are disbursed from loan repayment funds. Loan funds are disbursed to the local borrower agencies by the trustee bank as the local borrower agencies expend funds for the purposes of the loan and request reimbursement from the program. Interest is calculated from the date that funds are disbursed. Typically after the final disbursement has been made, the payment schedule is certified in the loan agreement and adjusted for the actual amounts disbursed. No provision for uncollectible accounts has been made as all loans are current in terms of compliance with the repayment schedules, and management believes that all loans will be repaid according to the terms of the loan agreements.

The drawn and outstanding principal balance of all loans guaranteed by the WPCSRF Program as of June 30, 2008, is \$144,511,963. The total loans receivable in the WPCSRF program includes \$129,375,594 presented as loans receivable and \$15,136,369 presented as advances to other funds. The advances are inter-fund loans within the DNRC used for the non-point source private loans program.

The drawn and outstanding principal balance of all loans guaranteed by the DWSRF Program as of June 30, 2008, is \$90,765,127. The total loans receivables in the DWSRF program includes \$89,969,216 presented as loans receivables and \$795,911 in advances. The advances are inter-fund loans within DNRC used to temporarily fund state match.

Loans mature at various intervals through July 1, 2038. The scheduled principal payments on loans and advances to other funds maturing in the years following state fiscal year (SFY) 2008 are as follows:

<u>SFY ending June 30:</u>	<u>WPCSRF Amount</u>	<u>DWSRF Amount</u>
2009	\$ 6,709,481	\$ 4,549,613
2010	9,511,900	5,228,580
2011	10,919,000	5,368,000
2012	10,583,100	5,472,500
2013 and thereafter	<u>106,788,482</u>	<u>70,146,434</u>
Total	\$ 144,511,963	\$ 90,765,127

As of June 30, 2008, the WPCSRF and DWSRF had authorized loans to public entities of the State of Montana that in the aggregate exceeded \$236.9 and \$122 million, respectively. The outstanding balances of the largest loans in each portfolio are as follows:

Water Pollution Control State Revolving Fund:

<u>Local Agency</u>	<u>Authorized Loan Amount</u>	<u>Outstanding Balance</u>
City of Kalispell	\$ 14,470,000	\$ 8,089,559
City of Great Falls	11,295,267	8,472,000
City of Helena	9,320,000	8,334,000
Big Sky/County Water & Sewer	7,000,000	5,869,000
Big Sky/County Water & Sewer	6,500,000	4,651,154
Big Sky/County Water & Sewer	5,513,000	2,081,000
City of Lewistown	5,400,000	4,614,000
City of Manhattan	4,757,000	4,483,434
Missoula WWTP	5,000,000	3,890,000
City of Missoula SID 524	<u>4,577,000</u>	<u>3,432,000</u>
Total	\$ 73,832,267	\$ 53,916,147

Drinking Water State Revolving Fund:

<u>Local Agency</u>	<u>Authorized Loan Amount</u>	<u>Outstanding Balance</u>
City of Billings	\$ 17,300,000	\$ 15,773,000
City of Havre II	8,401,000	7,031,000
City of Whitefish II	5,839,000	3,901,000
City of Laurel	5,250,000	3,138,000
Big Sky WSD*	5,000,000	3,087,277
City of Lewistown	3,549,000	2,943,000
City of East Helena	3,234,000	2,572,000
City of Great Falls	3,000,000	2,139,000
City of Helena	2,850,000	2,585,000
City of Helena II	<u>2,750,000</u>	<u>2,263,619</u>
Total	\$ 57,173,000	\$ 45,432,896

* Still drawing funds.

6. Interest Receivable

The interest receivable represents interest owed by borrowers as of June 30, 2008, for the July 1, 2008 payment. It represents the six months of interest accrued from the previous loan payment date of January 1, 2008. Interest receivable balances include \$321,036 in the WPCSRF Special Administration fund and \$1,245,651 in the WPCSRF Debt Service and Loan Loss Reserve funds; and \$232,003 in the DWSRF Special Administration fund and \$912,585 in the DWSRF Debt Service and Loan Loss Reserve funds. Interest receivable does not include interest payments received in June 2008 that were due July 1, 2008. Interest payments received during June 2008 amounted to \$1,239,811 for the WPCSRF and \$495,446 for the DWSRF.

7. Bonds Payable

Water Pollution Control SRF general obligation bonds payable at June 30, 2008, were as follows:

Series 1998A

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	3.75 – 5.15	\$ 915,000	\$ 90,118	\$ 1,005,118
2010		170,000	63,305	233,305
2011		180,000	55,165	235,165
2012		190,000	46,375	236,375
2013		195,000	37,038	232,038
2014-2016		<u>645,000</u>	<u>49,605</u>	<u>694,605</u>
Total Cash Requirements		\$ 2,295,000	\$ 341,606	\$ 2,636,606

Series 2000B

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.25 – 5.60	\$ 135,000	\$ 130,983	\$ 265,983
2010		145,000	124,086	269,086
2011		155,000	116,623	271,623
2012		160,000	108,668	268,668
2013		170,000	100,210	270,210
2014-2018		1,005,000	352,239	1,357,239
2019-2021		<u>760,000</u>	<u>65,213</u>	<u>825,213</u>
Total Cash Requirements		\$ 2,530,000	\$ 998,022	\$ 3,528,022

Series 2001H

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.00 – 5.00	\$ 115,000	\$ 94,295	\$ 209,295
2010		115,000	89,695	204,695
2011		120,000	84,920	204,920
2012		125,000	79,820	204,820
2013		130,000	74,400	204,400
2014-2018		755,000	274,458	1,029,458
2019-2022		<u>740,000</u>	<u>76,035</u>	<u>816,035</u>
Total Cash Requirements		\$ 2,100,000	\$ 773,623	\$ 2,873,623

Series 2003D

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	2.00 – 3.75	\$ 165,000	\$ 27,239	\$ 192,239
2010		170,000	23,426	193,426
2011		175,000	19,023	194,023
2012		180,000	14,050	194,050
2013		185,000	8,665	193,665
2014		190,000	2,945	192,945
Total Cash Requirements		\$ 1,065,000	\$ 95,348	\$ 1,160,348

Series 2004A

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	2.00 – 4.50	\$ 155,000	\$ 36,285	\$ 191,285
2010		160,000	32,148	192,148
2011		165,000	27,473	192,473
2012		165,000	22,316	187,316
2013		175,000	16,573	191,573
2014-2015		365,000	13,785	378,785
Total Cash Requirements		\$ 1,185,000	\$ 148,580	\$ 1,333,580

Series 2005G

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.00 – 4.75	\$ 115,000	\$ 79,990	\$ 194,990
2010		120,000	75,290	195,290
2011		120,000	70,490	190,490
2012		125,000	65,590	190,590
2013		135,000	60,390	195,390
2014-2018		755,000	208,575	963,575
2019-2021		540,000	35,328	575,328
Total Cash Requirements		\$ 1,910,000	\$ 595,653	\$ 2,505,653

TOTAL GENERAL OBLIGATION DEBT - WPCSRFPayable during the year
ending June 30,

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	\$ 1,600,000	\$ 458,910	\$ 2,058,910
2010	880,000	407,950	1,287,950
2011	915,000	373,694	1,288,694
2012	945,000	336,819	1,281,819
2013	990,000	297,276	1,287,276
2014-2018	3,715,000	901,607	4,616,607
2019-2022	<u>2,040,000</u>	<u>176,576</u>	<u>2,216,576</u>
Total Cash Requirements	\$ 11,085,000	\$ 2,952,832	\$ 14,037,832

Drinking Water SRF general obligation bonds payable at June 30, 2008, were as follows:

Series 1998FPayable during the year
ending June 30,

	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	3.60 – 4.85	\$ 150,000	\$ 90,855	\$ 240,855
2010		155,000	84,449	239,449
2011		160,000	77,675	237,675
2012		170,000	70,413	240,413
2013		175,000	62,649	237,649
2014-2018		1,010,000	179,564	1,189,564
2019		<u>230,000</u>	<u>5,578</u>	<u>235,578</u>
Total Cash Requirements		\$ 2,050,000	\$ 571,183	\$ 2,621,183

Series 2000APayable during the year
ending June 30,

	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.25 – 5.60	\$ 125,000	\$ 117,413	\$ 242,413
2010		130,000	111,132	241,132
2011		135,000	104,540	239,540
2012		145,000	97,467	242,467
2013		155,000	89,779	244,779
2014-2018		900,000	315,345	1,215,345
2019-2021		<u>680,000</u>	<u>58,244</u>	<u>738,244</u>
Total Cash Requirements		\$ 2,270,000	\$ 893,920	\$ 3,163,920

Series 2001G

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.00 – 5.00	\$ 135,000	\$ 112,265	\$ 247,265
2010		140,000	106,765	246,765
2011		145,000	100,974	245,974
2012		150,000	94,834	244,834
2013		155,000	88,351	243,351
2014-2018		895,000	326,194	1,221,194
2019-2022		<u>880,000</u>	<u>89,943</u>	<u>969,943</u>
Total Cash Requirements		\$ 2,500,000	\$ 919,326	\$ 3,419,326

Series 2003E

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	2.00 – 3.75	\$ 100,000	\$ 16,485	\$ 116,485
2010		105,000	14,150	119,150
2011		105,000	11,472	116,472
2012		110,000	8,460	118,460
2013		110,000	5,215	115,215
2014		<u>115,000</u>	<u>1,783</u>	<u>116,783</u>
Total Cash Requirements		\$ 645,000	\$ 57,565	\$ 702,565

Series 2005F

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.00 – 4.75	\$ 210,000	\$ 149,100	\$ 359,100
2010		215,000	140,600	355,600
2011		225,000	131,800	356,800
2012		235,000	122,600	357,600
2013		245,000	113,000	358,000
2014-2018		1,390,000	394,019	1,784,019
2019-2022		<u>995,000</u>	<u>67,744</u>	<u>1,062,744</u>
Total Cash Requirements		\$ 3,515,000	\$ 1,118,863	\$ 4,633,863

Series 2008 RAN

<u>Payable during the year ending June 30,</u>	<u>Interest Range (%)</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	4.25	\$ 0	\$ 0	\$ 0
2010		<u>650,000</u>	<u>21,941</u>	<u>671,941</u>
Total Cash Requirements		\$ 650,000	\$ 21,941	\$ 671,941

TOTAL GENERAL OBLIGATION DEBT - DWSRFPayable during the year
ending June 30,

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2009	\$ 720,000	\$ 486,118	\$ 1,206,118
2010	1,395,000	479,037	1,874,037
2011	770,000	426,461	1,196,461
2012	810,000	393,774	1,203,774
2013	840,000	358,994	1,198,994
2014-2018	4,310,000	1,216,905	5,526,905
2019-2022	<u>2,785,000</u>	<u>221,509</u>	<u>3,006,509</u>
Total Cash Requirements	\$ 11,630,000	\$ 3,582,798	\$ 15,212,798

8. Fund Balance

A portion, or all, of the fund balances in the WPCSRF and DWSRF have been reserved for Loans Receivable and Debt Service, indicating that a portion, or all, of the fund balances are not available for current expenditures.

9. Program Capitalization

The WPCSRF and DWSRF programs are capitalized by grants from the EPA and matching funds from the State of Montana. All grant funds drawn are recorded as revenue. As of June 30, 2008, the EPA has awarded capitalization grants of \$126,884,365 to the State of Montana for the WPCSRF program; \$230,681,347 has been drawn from federal and state funds for loans and administrative expenses. As of June 30, 2008, the EPA has awarded capitalization grants of \$102,206,788 to the State of Montana for the DWSRF program; \$118,689,924 has been drawn from federal and state funds for loans and administrative expenses. Montana has issued general obligation bonds, RANs, and BANs totaling \$25,490,000 for use as state matching funds for the WPCSRF program and \$16,095,000 for use as state matching funds in the DWSRF program.

10. Federal Capitalization Grant Revenues

Actual draws of federal funds differ from the amount of Federal Capitalization Grant Revenue reported on the Statement of Revenues, Expenditures and Changes in Fund Balance. This occurs because state accounting policy requires federal special revenue funds reflect a zero fund balance at fiscal year-end (with the exception of "A" accruals). Consequently, if a positive fund balance exists, deferred revenue is recorded. If a negative fund balance is reflected at fiscal year-end, an accounts receivable is established and revenue is recorded to zero the fund balance.

The following is a reconciliation of federal revenues reported on the financial statements to federal cash actually drawn during the state fiscal year:

WPCSRF

Federal Revenue - Combined Statement	\$4,714,484
Adjustment Due From Federal Govt FY07	0
Adjustment Deferred Revenue FY07	(153,360)
Adjustment Due From Federal Govt FY08	(6,254)
Adjustment Deferred Revenue FY08	375
Other Adjustments	0
Total Federal Draws	\$4,555,245

DWSRF

Federal Revenue - Combined Statement	\$7,888,901
Adjustment Due From Federal Govt FY07	10,564
Adjustment Deferred Revenue FY07	(95,520)
Adjustment Due From Federal Govt FY08	(181,112)
Adjustment Deferred Revenue FY08	270
Other Adjustments	(189)
Total Federal Draws	\$7,622,914

11. Interest Income on Investments

This revenue represents interest earnings on investments within the funds. All assets of the funds are fully invested by the trustee, to the degree possible, in investment vehicles. The investments range from U.S. Treasury obligation money market funds to long-term government securities. In some funds, interest income is earned in one fund but transferred to another fund in accordance with terms of the bond indenture.

12. Investment Appreciation/Gains (Depreciation/Losses)

This revenue represents unamortized (premiums) and discounts recognized upon maturity or disposal of government securities, as well as the change in unrealized appreciation and (depreciation) in the market value of investments as of June 30, 2008.

13. Interest Income from Loans

This revenue represents interest earnings from loan repayments made by borrowers. A typical loan carries an interest rate of 4%; however, during fiscal year 2004 the rate was decreased to 3.75% for new loans and the lower rate was continued through fiscal year 2008. The 3.75% interest rate is comprised of a loan interest rate of 2.00%, as well as a 1.00% Loan Loss Reserve fee and a 0.75% Special Administration fee. The interest income for each of these components totaled \$3,071,978, \$1,344,977, and \$1,077,058, respectively, for the WPCSRF program; and \$1,836,699, \$743,119, and \$656,702, respectively, for the DWSRF program. Disadvantaged communities can receive loans with an interest rate of 2.75% because no Loan Loss Reserve fee is levied.

14. Program Administration and Set-Aside Funds

This expenditure represents costs incurred by DEQ and DNRC to administer the SRF programs. This amount is limited to 4% of each grant award from the EPA. Program Administration appears under the Resource Development/Recreation function in the State of Montana Comprehensive Annual Financial Report (CAFR).

The DWSRF program includes several “sub-programs”, called set-asides, which states can elect. A State may use a certain portion of its capitalization grants for the following activities:

- up to 4 percent of its capitalization grants to administer the DWSRF and provide technical assistance to public water systems;
- up to 2 percent of its grants to provide assistance to small public water systems;
- up to 10 percent of its grants for state program management activities, including administration of the state public water system supervision program, administration of the source water protection program, development and implementation of the capacity development and operator certification programs;
- up to 15 percent of its grants to assist in the development and implementation of local drinking water protection initiatives and other State programs.

In the DWSRF, the 4 percent administrative set-aside must be deposited to a separate fund, and must have separate accounting and disclosure.

DWSRF Program Administration/Set-Asides Detail:

Administration - EPA Grants	\$319,439
Administration - State Funds	258,195
Technical Assistance	126,511
State Program Management	945,924
Local Assistance	124,404
Total Administration and Set-Asides	\$1,774,473

In the WPCSRF program, there are no set-aside funds available.

WPCSRF Program Administration Detail:

Administration - EPA Grants	\$129,754
Administration - State Funds	433,482
Total Administration	\$563,236

15. Other Financing Sources and Uses

The Recycled Transfer from the WPCSRF to the DWSRF represents the amount transferred between the two programs to fund drinking water project loans. At the discretion of the Governor, the state may transfer up to 33 percent of the WPCSRF capitalization grant to the DWSRF or an equal amount from the DWSRF to the WPCSRF. The transferred funds are “recycled” such that they consist of principal repayments from previous loans.

The Debt Service Sweep represents loan interest amounts received that exceed the debt service requirements. The balances remaining in Debt Service funds are transferred to Investment accounts in State Special Revenue funds. Both funds are required by the State Revolving Fund Program. This occurs after payments are made to the bondholders on July 15 of each year. In the Arbitrage Certificate, this activity is termed a Debt Service Sweep.

The Loan Loss Reserve Sweep represents cash in excess of the reserve requirement that is transferred from the Loan Loss Reserve funds to the Principal funds per the bond indentures. The Loan Loss Reserve funds are not required by the State Revolving Fund Program, but the state elected to have these funds to account for these transactions separately.

The Federal Capitalization Grant represents the transfer of EPA grant funds from federal special revenue funds to the Loan Accounts in state special revenue funds to fund first round loans.

The Bond/RAN/BAN Proceeds represents the non-cash transfer of INTERCAP loan payables from Loan Proceeds Accounts in state special revenue funds to the funds responsible for repayment of the debt in debt service funds.

16. Subsequent Events

In September 2008, a RAN was issued for \$700,000 to the WPCSRF. In December 2008, an additional \$200,000 was drawn on the 2008 DWSRF RAN. These RANs are to match EPA Capitalization Grant funds.

LEGISLATIVE AUDIT DIVISION

B-1

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel



Deputy Legislative Auditors
James Gillett
Angie Grove

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements. The Montana Water Pollution Control and Drinking Water Schedule of Revolving and Non-Revolving SRF Programs Balance Sheet, Special Revenue and Debt Service Funds, Regulatory Basis, as of June 30, 2008, and the related Schedule of Revolving and Non-Revolving SRF Program Revenues, Expenditures, and Changes in Fund Balances, Special Revenue and Debt Service Funds, Regulatory Basis, for the year then ended are presented for the purposes of additional analysis and are not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the programs' financial statements and, in our opinion, is fairly stated in all material respects in relation to the programs' financial statements taken as a whole.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

January 15, 2009

**MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAMS
BALANCE SHEET
SPECIAL REVENUE AND DEBT SERVICE FUNDS
REGULATORY BASIS
June 30, 2008**

	WATER POLLUTION CONTROL SPECIAL REVENUE		WATER POLLUTION CONTROL DEBT SERVICE FUND		DRINKING WATER SPECIAL REVENUE		DRINKING WATER DEBT SERVICE FUND		(MEMORANDUM ONLY) TOTAL
	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	
ASSETS									
Cash and Cash Equivalents	\$18,380,030	\$703,138	\$1,079,494	\$1,584,970	\$5,519,953	\$2,101,876	\$371,545	\$1,301,110	\$31,042,115
Interest Receivable		321,036	862,736	382,915		232,003	627,869	276,129	2,702,688
Accounts Receivable	25,734	32			30,432		5,701	2,886	64,785
Due from Federal Government	6,254				181,112				187,366
Due from Other Fund/Business Unit	25,153								25,153
Loans Receivable	129,375,594				89,969,216				219,344,810
Advances to Other Funds	15,136,369								15,136,369
Total Assets	\$162,949,133	\$1,024,206	\$1,942,230	\$1,967,885	\$95,700,714	\$2,333,879	\$1,005,115	\$1,580,125	\$268,503,287
LIABILITIES AND FUND BALANCES									
Liabilities:									
Accounts Payable	\$206,421		\$245		\$267,990				\$474,656
Payroll Payable	6,408	\$10,326			66,156	\$5,220			88,110
Interest Payable	18,961	32,500			72,592			(\$3,096)	120,957
Due to Other BU or Fund					25,153		\$5,568		30,721
Deferred Revenue	375				269				644
Loans Payable							650,000		650,000
Total Liabilities	\$232,166	\$42,826	\$245	\$0	\$432,160	\$5,220	\$655,568	(\$3,096)	\$1,365,088
Fund Balances									
Reserved for LT Loans/Notes/Advances	\$144,511,963				\$89,969,216				\$234,481,179
Reserved for Debt Service			\$1,941,986	\$1,967,885			\$349,547	\$1,583,221	5,842,638
Unreserved, Undesignated	18,205,004	981,380			5,299,337	2,328,659			26,814,381
Total Fund Balances	162,716,967	981,380	\$1,941,986	\$1,967,885	\$95,268,553	\$2,328,659	\$349,547	\$1,583,221	\$267,138,198
Total Liabilities and Fund Balances	\$162,949,133	\$1,024,206	\$1,942,230	\$1,967,885	\$95,700,713	\$2,333,879	\$1,005,115	\$1,580,125	\$268,503,286

This schedule is prepared on a regulatory basis of presentation, rather than a GAAP (1) basis, as requested by the Environmental Protection Agency (EPA) for the Water Pollution Control and Drinking Water State Revolving Fund (SRF) Programs. This presentation separates certain regulated Revolving Fund (within the Fund) and Non-Revolving Fund (outside the Fund) activity by fund type. All proceeds from the EPA Capitalization Grant, corresponding state matching funds, and loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act and Title XIV of the Safe Drinking Water Act. Other proceeds, including Administration and Origination Fees and Loan Loss Reserves are deposited into the Non-Revolving Fund and may be used for other water quality purposes under the federal acts mentioned above.

(1) Generally Accepted Accounting Principles (GAAP).

**MONTANA WATER POLLUTION CONTROL AND DRINKING WATER
SCHEDULE OF REVOLVING AND NON-REVOLVING SRF PROGRAM
REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
SPECIAL REVENUE AND DEBT SERVICE FUNDS
REGULATORY BASIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2008**

	WATER POLLUTION CONTROL SPECIAL REVENUE		WATER POLLUTION CONTROL DEBT SERVICE FUND		DRINKING WATER SPECIAL REVENUE		DRINKING WATER DEBT SERVICE FUND		(MEMORANDUM ONLY) TOTAL
	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	REVOLVING FUND	NON REVOLVING FUND	
REVENUES:									
Federal Capitalization Grant Revenue	\$4,714,484				\$7,888,901				\$12,603,385
Interest Income from Investments	568,818	\$112,660	\$18,029	\$46,384	151,281	\$63,060	\$5,982	\$36,553	1,002,768
Investment Appreciation/Gains (Depreciation/Losses)	(71,448)	71,106			2,243	2,484		244	4,628
Interest Income from Loans	0	1,077,058	3,071,978	1,344,977	0	656,702	1,836,699	743,119	8,730,533
Other Income		4			189	36			229
Total Revenues	\$5,211,854	\$1,260,827	\$3,090,007	\$1,391,361	\$8,042,614	\$722,283	\$1,842,681	\$779,916	\$22,341,543
EXPENDITURES:									
Program Administration/Set-Asides	\$154,396	\$408,835	\$3,543		\$1,516,278	\$258,195			\$2,341,248
Total Expenditures	\$154,396	\$408,835	\$3,543	\$0	\$1,516,278	\$258,195	\$0	\$0	\$2,341,248
Excess Revenues Over/(Under) Expenditures	\$5,057,458	\$851,992	\$3,086,464	\$1,391,361	\$6,526,336	\$464,088	\$1,842,681	\$779,916	\$20,000,296
OTHER FINANCING SOURCES:									
<i>Operating Transfers In:</i>									
Recycled Transfer from Water Pollution Control					\$2,500,000				2,500,000
Debt Service Sweep	\$612,283				584,350				\$1,196,632
Loan Loss Reserve Sweep	1,463,012				754,644				2,217,655
Special Administration Transfer	3,556,484								3,556,483
Bond/RAN/BAN Proceeds	900,000				1,300,000				2,199,999
Investment Earnings from State Special Revenue		\$25	\$6,298			\$27	\$101,166		107,514
Total Other Financing Sources	\$6,531,779	\$25	\$6,298	\$0	\$5,138,994	\$27	\$101,166	\$0	\$11,778,283
OTHER FINANCING USES:									
Bond Principal			\$1,870,000				\$690,000		\$2,560,000
Bond Interest			531,285				520,854		1,052,139
Loan Interest			7,924				7,240		15,164
Cost of Issuance	\$11,500				\$12,500				24,000
<i>Operating Transfers Out:</i>									
Debt Service Sweep			612,283				584,350		1,196,632
Loan Loss Reserve Sweep				\$1,463,012				\$754,644	2,217,656
Special Administration Transfer		\$3,556,484							3,556,484
Recycled Transfer to Drinking Water	2,500,000								2,500,000
Bond/RAN/BAN Proceeds			900,000				1,300,000		2,200,000
Investment Earnings to Debt Service	6,322				101,193				107,515
Total Other Financing Uses	\$2,517,822	\$3,556,484	\$3,921,492	\$1,463,012	\$113,693	\$0	\$3,102,444	\$754,644	\$15,429,590
Excess (deficiency) of Revenues and Other Financing Sources over (under) Expenditures and Other Financing Uses	\$9,071,415	(\$2,704,468)	(\$828,730)	(\$71,651)	\$11,551,637	\$464,114	(\$1,158,597)	\$25,272	\$16,348,989
Fund Balances July 1, 2007	\$153,630,733	\$3,685,848	\$2,770,715	\$2,039,536	\$83,716,916	\$1,864,544	\$1,538,125	\$1,557,953	\$250,804,370
Prior Year Adjustments	14,820	0	1	(0)	0	0	(29,981)	(4)	(15,164)
Fund Balances June 30, 2008	\$162,716,967	\$981,380	\$1,941,986	\$1,967,885	\$95,268,553	\$2,328,659	\$349,547	\$1,583,221	\$267,138,198

This schedule is prepared on a regulatory basis of presentation, rather than a GAAP (1) basis, as requested by the Environmental Protection Agency (EPA) for the Water Pollution Control and Drinking Water State Revolving Fund (SRF) Programs. This presentation separates certain regulated Revolving Fund (within the Fund) and Non-Revolving Fund (outside the Fund) activity by fund type. All proceeds from the EPA Capitalization Grant, corresponding state matching funds, and loan principal and interest repayments must be deposited into the Revolving Fund under Title VI of the Clean Water Act and Title XIV of the Safe Drinking Water Act. Other proceeds, including Administration and Origination Fees and Loan Loss Reserves are deposited into the Non-Revolving Fund and may be used for other water quality purposes under the federal acts mentioned above.

(1) Generally Accepted Accounting Principles (GAAP).

Tori Hunthausen, Legislative Auditor
Monica Huyg, Legal Counsel



Deputy Legislative Auditors
James Gillett
Angie Grove

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

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the financial statements of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs as of and for the fiscal year ended June 30, 2008, and have issued our report thereon dated January 15, 2009. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the programs' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the programs' internal control over financial reporting.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph of this section and would not necessarily identify all deficiencies in internal

control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified a deficiency in internal control over financial reporting that we consider to be a significant deficiency.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency described below to be a significant deficiency in internal control over financial reporting.

1. The Montana Water Pollution Control and Drinking Water State Revolving Fund Programs did not accurately compile its notes to the financial statements, in accordance with generally accepted accounting principles, due to ineffective controls to prevent or detect and correct material errors in the note disclosures in a timely manner.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, the significant deficiency described above, we consider to be a material weakness.

This report is intended solely for the information and use of the Legislative Audit Committee, the departments' management, the Montana State Legislature, and the federal Environmental Protection Agency and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Respectfully submitted,

/s/ James Gillett

James Gillett, CPA
Deputy Legislative Auditor

January 15, 2009

DEPARTMENT OF NATURAL RESOURCES
AND CONSERVATION

D-1



BRIAN SCHWEITZER, GOVERNOR

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STATE OF MONTANA

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February 19, 2009

Tori Hunthausen
Legislative Auditor
Room 160, State Capitol
Helena, MT 59620-1705

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FEB 19 2009

LEGISLATIVE AUDIT DIV.

Dear Mrs. Hunthausen:

We have received and reviewed the financial audit of the Montana Water Pollution Control and Drinking Water State Revolving Fund Programs for the fiscal year ended June 30, 2008. We are pleased with the unqualified opinion and wish to thank your staff for the professionalism and courtesy with which the audit was conducted.

Please find below the agencies' response to the deficiency identified to be significant in the Internal Controls over financial reporting.

The Montana Water Pollution Control State Revolving Fund Program did not accurately compile its notes to the financial statements, in accordance with generally accepted accounting principles, due to ineffective controls to prevent or detect and correct material errors in the note disclosures in a timely manner.

The departments concur and will continue working together to improve processes, internal accounting controls, monitoring, and reporting practices.

Sincerely,

Handwritten signature of Mary Sexton in black ink.

Mary Sexton, Director - DNRC

Handwritten signature of Ann Bauchman in black ink.

Ann Bauchman, Centralized Services Division Administrator - DNRC

Handwritten signature of Richard Oppen in black ink.

Richard Oppen, Director - DEQ

Handwritten signature of Dean Rude in black ink.

Dean Rude, Chief Financial Officer - DEQ

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