

**AUDIT REPORT  
OF THE  
NEBRASKA DEPARTMENT OF  
ENVIRONMENTAL QUALITY  
CLEAN WATER  
STATE REVOLVING FUND PROGRAM  
JULY 1, 2005 THROUGH JUNE 30, 2006**

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**Issued on April 17, 2007**

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. Section 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 and privately 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 be used for the purposes of 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, 2006, the EPA had awarded nearly \$120 million in capitalization grants to the State. The award of this \$120 million required the State to contribute approximately \$24 million in matching funds. The State provided appropriations to contribute \$955 thousand 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.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
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**EXIT CONFERENCE**

An exit conference was held March 21, 2007, with the Department to discuss the results of our examination. Those in attendance for the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program were:

| <b>NAME</b>   | <b>TITLE</b>    |
|---------------|-----------------|
| Tom Lamberson | Deputy Director |

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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**INDEPENDENT AUDITORS' REPORT**

Nebraska Department of Environmental Quality  
Lincoln, Nebraska

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, 2006, 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 present only the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program and are not intended to present fairly the financial position and results of operations of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program 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 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, 2006, 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 21, 2007, 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, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of 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.

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 21, 2007, 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.

Our audit was performed for the purpose of forming an opinion on the financial statements of the Program taken as a whole. Management's Discussion and Analysis is presented for purposes of additional analysis and is not a required part of the basic financial statements. The Management's Discussion and Analysis has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on them.

Pat Reding, CPA

Assistant Deputy Auditor

March 21, 2007

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)**

This section of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program's (Program) financial report presents a narrative overview and analysis of the financial activities of the Program for the fiscal year ended June 30, 2006. This analysis has been prepared by management of the Department and is intended to be read with the financial statements and related footnotes that follow this section.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This discussion and analysis is intended to serve as an introduction to the Program's basic financial statements. The Program's basic financial statements include: 1) Balance Sheet, 2) Statement of Revenues, Expenses, and Changes in Net Assets, 3) Statement of Cash Flows, and 4) Notes to Financial Statements.

The Balance Sheet presents information on all of the Program's assets and liabilities, with the difference between the two reported as net assets.

The Statement of Revenues, Expenses, and Changes in Net Assets presents information showing how the Program's net assets changed during the most recent fiscal year.

The Statement of Cash Flows presents the Program's flows of cash by defined categories. The primary purpose of the Statement of Cash Flows is to provide information about the Program's cash receipts and payments during the year.

The Notes to Financial Statements provide additional information that is essential to a full understanding of the data provided in the financial statements.

**ANALYSIS OF BALANCES AND TRANSACTIONS OF ENTERPRISE FUND**

**Changes in Net Assets**

For the fiscal year ended June 30, 2006, net assets of the Program increased by 7%.

|                               | <u>2006</u>           | <u>2005</u>           |
|-------------------------------|-----------------------|-----------------------|
| <b>Current Assets</b>         | \$ 49,714,206         | \$ 62,339,906         |
| <b>Noncurrent Assets</b>      | 115,033,828           | 90,666,648            |
| Total Assets                  | <u>164,748,034</u>    | <u>153,006,554</u>    |
| <b>Current Liabilities</b>    | 1,616,055             | 307,085               |
| <b>Noncurrent Liabilities</b> | -                     | -                     |
| Total Liabilities             | <u>1,616,055</u>      | <u>307,085</u>        |
| <b>Net Assets</b>             |                       |                       |
| Unrestricted                  | 163,131,979           | 152,699,469           |
| Total Net Assets              | <u>\$ 163,131,979</u> | <u>\$ 152,699,469</u> |

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)**

(Continued)

|                                      | <u>2006</u>           | <u>2005</u>           |
|--------------------------------------|-----------------------|-----------------------|
| <b>Loan Fees Administration</b>      | \$ 1,029,329          | \$ 816,037            |
| <b>Interest</b>                      | 5,088,744             | 4,855,097             |
| <b>Miscellaneous Revenue</b>         | -                     | 49                    |
| Total Operating Revenues             | 6,118,073             | 5,671,183             |
| <b>Administration</b>                | 1,121,808             | 1,074,054             |
| <b>Bond Expenses</b>                 | 31,055                | (22)                  |
| Total Operating Expenses             | 1,152,863             | 1,074,032             |
| <b>Operating Income</b>              | 4,965,210             | 4,597,151             |
| <b>Capital Federal Grants</b>        | 5,467,300             | 8,417,835             |
| <b>Change in Net Assets</b>          | 10,432,510            | 13,014,986            |
| <b>Net Assets, Beginning of Year</b> | 152,699,469           | 139,684,483           |
| <b>Net Assets, End of Year</b>       | <u>\$ 163,131,979</u> | <u>\$ 152,699,469</u> |

The significant changes from the fiscal year ended June 30, 2005, to the fiscal year ended June 30, 2006 include a decrease in Cash, an increase in Loans Receivable, an increase in Bonds Payable, and a decrease in Federal Capitalization grants.

The capitalization grants received from the EPA have shown a steady decline the past few years. Fiscal year 2006 was no different. The amount received went from \$8.4 million to \$5.4 million. The program made \$33.75 million dollars in loan payments to recipients during the fiscal year. This amount is above and beyond the amount of the capitalization grant received. This required the use of repaid principal to be used to fund the payments. This repaid principal is recorded as Cash on the balance sheet. Due to the timing of the bond issues necessary to meet the match requirement of the capitalization grants, the Department issued two bond series during the fiscal year. Including the upfront interest and cost of issue fees, the Department transferred to the trustee \$1.6 million dollars. The loans receivable balance increased \$24.3 million. Loans to three communities resulted in \$15.7 million of the increase between 2005 and 2006; they are McCook, North Platte, and Omaha.

See the Notes to Financial Statements for additional discussion of loans receivable.

### **ECONOMIC OUTLOOK**

No conditions were noted that would be expected to have a significant effect on the financial position or results of operations of the Program.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
 CLEAN WATER STATE REVOLVING FUND PROGRAM  
**BALANCE SHEET**  
 June 30, 2006

|   | <u>Enterprise Fund</u>       |
|---|------------------------------|
| <b>ASSETS</b>                           |                              |
| CURRENT ASSETS                          |                              |
| Cash in State Treasury (Note 2)         | \$ 39,443,466                |
| Amounts Held by Trustee (Note 2)        | 1,637,700                    |
| Administrative Fees Receivable          | 2,904                        |
| Loan Interest Receivable                | 15,035                       |
| Interest Receivables                    | 174,241                      |
| Loans Receivable - Current (Note 3)     | 8,440,860                    |
| <b>TOTAL CURRENT ASSETS</b>             | <u>49,714,206</u>            |
| NON-CURRENT ASSETS                      |                              |
| Loans Receivable (Note 3)               | 115,033,828                  |
| <b>TOTAL NON-CURRENT ASSETS</b>         | <u>115,033,828</u>           |
| <b>TOTAL ASSETS</b>                     | <u><u>\$ 164,748,034</u></u> |
| <br><b>LIABILITIES</b>                  |                              |
| CURRENT LIABILITIES                     |                              |
| Accrued Bond Interest Payable           | \$ 31,055                    |
| Bonds Payable - Current (Note 4)        | 1,585,000                    |
| <b>TOTAL CURRENT LIABILITIES</b>        | <u>1,616,055</u>             |
| <b>TOTAL LIABILITIES</b>                | <u>1,616,055</u>             |
| <br><b>NET ASSETS</b>                   |                              |
| Unrestricted                            | 163,131,979                  |
| <b>TOTAL NET ASSETS</b>                 | <u>163,131,979</u>           |
| <b>TOTAL LIABILITIES AND NET ASSETS</b> | <u><u>\$ 164,748,034</u></u> |

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

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
 CLEAN WATER STATE REVOLVING FUND PROGRAM  
**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS**  
 For the Year Ended June 30, 2006

|  | <u>Enterprise Fund</u> |
|--|------------------------|
| <b>OPERATING REVENUES:</b>                               |                        |
| Loan Fees Administration (Note 6)                        | \$ 1,029,329           |
| Interest on Loans  | 3,082,919              |
| Interest on Fund Balance - Trustee                       | 31,050                 |
| Interest on Fund Balance - State Operating Pool (Note 7) | 1,974,775              |
| <b>TOTAL OPERATING REVENUES</b>                          | <b>6,118,073</b>       |
| <b>OPERATING EXPENSES:</b>                               |                        |
| Administrative Costs                                     | 705,599                |
| Small Town Grants (Note 8)                               | 363,249                |
| Hardship Grant Payments                                  | 18,294                 |
| Facility Plan Grants                                     | 34,666                 |
| Interest Expense - State Match Bonds                     | 31,055                 |
| <b>TOTAL OPERATING EXPENSES</b>                          | <b>1,152,863</b>       |
| <b>OPERATING INCOME</b>                                  | 4,965,210              |
| <b>CAPITAL CONTRIBUTIONS - FEDERAL GRANTS</b>            | <b>5,467,300</b>       |
| <b>CHANGE IN NET ASSETS</b>                              | 10,432,510             |
| <b>TOTAL NET ASSETS, BEGINNING OF YEAR</b>               | <b>152,699,469</b>     |
| <b>TOTAL NET ASSETS, END OF YEAR</b>                     | <b>\$ 163,131,979</b>  |

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

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM  
**STATEMENT OF CASH FLOWS**  
For the Year Ended June 30, 2006

|   | <u>Enterprise Fund</u> |
|---|------------------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                        |
| Receipts From Customers   | \$ 11,873,084          |
| Bonds Issued  | 1,585,000              |
| Interest on Investments   | 2,006,789              |
| Payments to Borrowers   | (34,478,179)           |
| Payments to Employees and Vendors   | (705,599)              |
| Payments to Investments   | (1,637,700)            |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>  | <u>(21,356,605)</u>    |
| <b>CASH FLOWS FROM NON-CAPITAL &amp; RELATED FINANCING ACTIVITIES:</b>                                |                        |
| Funds Received From the Environmental Protection Agency   | <u>5,467,300</u>       |
| <b>NET CASH FROM NON-CAPITAL &amp; RELATED FINANCING ACTIVITIES:</b>                                  | 5,467,300              |
| <b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>   | <u>55,332,771</u>      |
| <b>CASH AND CASH EQUIVALENTS, END OF YEAR</b>   | <u>\$ 39,443,466</u>   |
| <br><b>RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES:</b>    |                        |
| Operating Income  | \$ 4,965,210           |
| <b>ADJUSTMENTS TO RECONCILE OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY OPERATING ACTIVITIES:</b> |                        |
| (Increase)/Decrease in Loans Receivable   | (25,976,110)           |
| (Increase)/Decrease in Amounts Held by Trustee  | (1,637,700)            |
| (Increase)/Decrease in Interest Receivables   | 964                    |
| Increase/(Decrease) in Bonds Payable  | 1,585,000              |
| Increase/(Decrease) in Accrued Bond Interest Payable  | 31,055                 |
| Increase/(Decrease) in Administrative Fees Receivable   | (2,904)                |
| Increase/(Decrease) in Loan Interest Receivable   | (15,035)               |
| Increase/(Decrease) in Accounts Payable   | <u>(307,085)</u>       |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>  | <u>\$ (21,356,605)</u> |

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

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

For the Fiscal Year Ended June 30, 2006

**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 conformity with accounting principles generally accepted in the United States of America (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 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  
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**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. It includes the following funds as identified in the Wastewater Treatment Facilities Construction Assistance Act:

- Clean Water Facilities Funds – General Fund 10000, Federal Funds 48412 and 48413, and Bond Funds 68470, 68471, 68472, and 68473.
- Administration Funds – Cash Funds 28460, 28461, and 28462.

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

The activity of these ten 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 the Program will be available in perpetuity as intended.

This fund classification differs from the classification used in the State of Nebraska's Comprehensive Annual Financial Report (CAFR). The CAFR classifies the Cash funds, Federal funds, and Bond funds as Special Revenue funds because the major source of revenue is Federal assistance.

- D. Measurement Focus, 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.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

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

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.

**E. Cash and Cash Equivalents.** Cash in State Treasury is considered cash equivalents due to its liquid nature.

**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 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 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 2.5% to 5.25% 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, 2006, which was collectible in fiscal year 2007.

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.** The Nebraska Information System (NIS) has the capability of showing the amount of accounts payable at any time. The amount shown at June 30, 2006, is the figure that was used for this amount.

**H. Restricted Net Assets.** When both restricted and unrestricted resources are available for use, it is the Department's policy to use restricted resources first, then unrestricted resources, as they are needed. Net assets are reported as restricted when they are held in a separate account that can be used to pay debt principal and interest only and cannot be used to pay other current liabilities.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

NOTES TO FINANCIAL STATEMENTS

(Continued)

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

I. **Use of Estimates.** The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at fiscal-year-end and revenues and expenditures during the reporting period. Actual results could differ from those estimates.

2. **Cash in State Treasury and Amounts Held by Trustee**

**Cash in State Treasury.** Cash in State Treasury represents the cash balance as reflected on NIS. Investment of all available cash is made by the State Investment Officer on a daily basis, based on total bank balances. These funds are held in the State of Nebraska Operating Investment Pool (OIP), an internal investment pool. Additional information on the deposits and investments portfolio including investment policies, risks, and types of investments can be found in the State of Nebraska's Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2006. All funds of the Clean Water State Revolving Fund Program were designated for investment during the fiscal year ended June 30, 2006.

**Amounts Held by Trustee.** The Nebraska Investment Finance Authority (NIFA) (the "Issuer") issues revenue bonds, the proceeds which are used by the Department to provide the 20% match requirements for the Department's Federal Capitalization Grants (See Note 4, Bonds Payable, for more details on these bonds). Wells Fargo Bank Iowa, National Association, (Trustee), as trustee, establishes the appropriate accounts and invests the monies in accordance with the Bond Indenture. At June 30, 2006, the amount held by the Trustee of \$1,637,700, stated at Fair Value, was invested in U.S. bonds and notes. The Program's investments at June 30, 2006, are as follows.

| Debt Securities     | Fair Value   | Interest Rate | Call Date |
|---------------------|--------------|---------------|-----------|
| U.S. Treasury Notes | \$ 901,000   | 4.14%         | 9/29/2006 |
| U.S. Treasury Notes | 736,700      | 4.89%         | 5/15/2007 |
| Total               | \$ 1,637,700 |               |           |

For an investment, custodial credit risk is the risk that, in the event of the failure of the counterparty, the Program will not be able to recover the value of its investments that are in the possession of an outside party. The Amounts Held by Trustee was uninsured and held by and in the name of the Trustee, not in the name of the Program.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

**3. Loans Receivable**

As of June 30, 2006, the Program had 125 outstanding loans with communities that totaled \$123,474,688. The outstanding balances of the ten communities with the largest SRF debt, which represent 55.3% of the total loans, were as follows:

| City         | Outstanding<br>Balance |
|--------------|------------------------|
| Omaha        | \$ 29,991,203          |
| Gibbon       | 6,172,180              |
| North Platte | 5,311,639              |
| West Point   | 5,021,412              |
| Scottsbluff  | 4,943,835              |
| Valley       | 4,401,669              |
| Wahoo        | 4,191,308              |
| Gering       | 3,250,000              |
| Fremont      | 2,542,312              |
| Falls City   | 2,451,446              |
| Total        | \$ 68,277,004          |

**4. Bonds Payable**

The Environmental Protection Agency (EPA) requires the Program to provide matching funds. During the fiscal year, the Program issued \$1,585,000 in short-term revenue bonds to meet this requirement.

The State has entered into a special financing arrangement with NIFA, an independent instrumentality of the State exercising essential public functions, to provide matching funds for the State's Clean Water Program. The Series 2005B and Series 2006B Bonds are limited obligations of NIFA, payable only from and secured only by the Trust Estate. The Series 2005B and Series 2006B Bonds are revenue bonds. The Series 2005B and 2006B Bonds shall not constitute a debt, liability, general obligation of the State, or a pledge of the faith and Credit of the State, but are payable solely out of the revenue or money NIFA pledged to the Trust Estate. Neither the faith and credit nor the taxing power of the State is pledged for the payment of the principal of, premium, if any, or the interest on the Series 2005B and Series 2006B Bonds. The current bonds payable amount was determined using the amount of bond principal to be retired in fiscal year 2007. Bonds payable for the fiscal year ended June 30, 2006, is as follows:

|               | Beginning<br>Balance | Additions   | Retirements | Ending<br>Balance | Current<br>Portion |
|---------------|----------------------|-------------|-------------|-------------------|--------------------|
| Bonds Payable | \$ -                 | \$1,585,000 | \$ -        | \$1,585,000       | \$1,585,000        |

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

**4. Bonds Payable** (Concluded)

Bonds payable at June 30, 2006, consist of the following:

| Series | Original<br>Issue | Retirement | 2006 Balance | Interest Rates | Final<br>Maturity Date |
|--------|-------------------|------------|--------------|----------------|------------------------|
| 2005B  | \$ 875,000        | \$ -       | \$ 875,000   | 3.18%          | October 1, 2006        |
| 2006B  | \$ 710,000        | \$ -       | \$ 710,000   | 3.62%          | May 15, 2007           |

**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, 2006.

| 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             | 6,855,000             | -           |
| 2003   | 7,069,900             | 7,069,900             | -           |
| 2004   | 6,747,100             | 6,747,100             | -           |
| 2005   | 5,467,300             | 5,467,300             | -           |
| Totals | <u>\$ 119,741,097</u> | <u>\$ 119,741,097</u> | <u>\$ -</u> |

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

|                                   |                       |
|-----------------------------------|-----------------------|
| Contributed Capital July 1, 2005  | \$ 115,228,797        |
| Contributed During the Year       |                       |
| Funds Received From EPA           | 5,467,300             |
| Contributed Capital June 30, 2006 | <u>\$ 120,696,097</u> |

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

5. **Net Assets** (Concluded)

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 the fiscal years ended June 30, 1989, and 1990, respectively.

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, \$218,692 will be used as match for the fiscal year 2005 capitalization grant, and \$176,972 will be used as match for the fiscal year 2006 capitalization grant.

7. **Interest on Fund Balance – State Operating Pool**

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 5,000 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 small town grants. Interest expenses are also operating expenses since making loans is the primary purpose of the Program.

10. **State Employee's Retirement Plan (Plan)**

The single-employer plan became effective by statute on January 1, 1964. Prior to January 1, 2003, the plan consisted of a defined contribution plan that covered State employees. Effective January 1, 2003, a cash balance benefit was added to the State

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

**10. State Employee's Retirement Plan (Plan)** (Continued)

Employees Retirement Act. The cash balance benefit is a type of defined benefit plan. Each member employed and participating in the retirement system prior to January 1, 2003, elected to either continue participation in the defined contribution benefit or begin participation in the cash balance benefit. The defined contribution benefit is closed to new entrants. All new members of the Plan on and after January 1, 2003, become members of the cash balance benefit. The benefits and funding policy of the Plan is established and can only be amended by the Nebraska Legislature.

All permanent full-time employees who have 12 continuous months of service are required to begin participation in the retirement system. All permanent full-time or permanent part-time employees who have 12 months of service within a five-year period, and who have attained the age of 20, may exercise the option to begin participation in the retirement system.

**Contribution.** Each member contributes 4.33% of his or her monthly compensation until \$864 has been contributed and 4.8% of pay for the rest of the calendar year. The Department matches the member's contribution at a rate of 156%. The employee's and employer's contributions are kept in separate accounts.

The employee's account is fully vested. The employer's account is vested 100% after a total of three years of participation in the system, including the twelve-month eligibility period or credit for participation in another governmental plan prior to actual contribution to the Plan.

**Defined Contribution Benefit.** Upon attainment of age 55, regardless of service, the retirement allowance shall be equal to the sum of the employee and employer account. Members have several forms of payment available, including withdrawals, deferrals, annuities, or a combination of these.

Effective January 1, 2007, retirement plan membership is mandatory for all full-time employees immediately upon date of hire. Retirement plan membership is voluntary for part-time employees who have attained the age of twenty. An employee may retire after age 55 with five years of State service, or any time after age 65. Contributions to State retirement will be at the rate of 4.8%. The State contributes 156% of the employee contribution. The employee's account is fully vested. The employer's account is vested 100% after a total of three years of participation in the system, or credit for participation in another governmental plan prior to actual contribution to the Plan.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

**10. State Employee's Retirement Plan (Plan)** (Concluded)

**Cash Balance Benefit.** Upon attainment of age 55, regardless of service, the retirement allowance shall be equal to the accumulated employee and employer cash balance accounts, including interest credits, annuitized for payment in the normal form. The normal form of payment is a single life annuity with five year certain, payable monthly. Members will have the option to convert their member cash balance account to a monthly annuity with built in cost-of-living adjustments of 2.5% annually. Also available are additional forms of payment allowed under the Plan which are actuarially equivalent to the normal form, including the option of lump-sum or partial lump-sum.

For the fiscal year ended June 30, 2006, the Clean Water State Revolving Fund Program's employees contributed \$16,619 and the Department contributed \$25,926. A separate plan report is issued and can be obtained from the Nebraska Public Employees Retirement System. This report contains full pension-related disclosures.

**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, and natural disasters. 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 with the exception of the health and life insurance programs which are maintained by the DAS Personnel Division. The State has chosen to purchase insurance for:

- A. Motor vehicle liability, which is insured for the first \$5 million of exposure per accident with a self-insured retention of \$300,000 per accident, except for accidents involving vehicular pursuit which have a \$1,000,000 self-insured retention per accident. Insurance is also purchased for medical payments, physical damage, and uninsured and underinsured motorists with various limits and deductibles. State agencies have the option to purchase coverage for physical damage to vehicles.
- B. Health care and life insurance for eligible employees.
- C. Crime coverage, with a limit of \$1 million for each loss, and a \$25,000 self-insured retention per incident was in effect from July 1, 2005, through October 18, 2005. Starting October 19, 2005, the limit for each loss was increased to \$21 million.

NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM

**NOTES TO FINANCIAL STATEMENTS**

(Continued)

**11. Contingencies and Commitments** (Concluded)

- D. Real and personal property on a blanket basis for losses up to \$250,000,000, with a self-insured retention of \$200,000 per loss occurrence. Newly acquired properties are covered up to \$5,000,000 for 90 days or until the value of the property is reported to the insurance company. The perils of flood, earthquake, and acts of terrorism have various coverages, sublimits, and self insurance. Details of these coverages are available from the Department of Administrative Services Risk Management Division. State agencies have the option to purchase building contents and inland marine coverage.

No settlements exceeded commercial insurance coverage in any of the past three fiscal years. Health care insurance is funded in the Compensation Insurance Trust Fund through a combination of employee and State contributions. Workers' compensation is also funded in the Workers' Compensation Internal Service Fund through assessments on each agency based on total agency payroll and past experience. Tort claims, theft of, damage to, or 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. Reconciliation of Bank Records to the Nebraska Information System**

Through their bank reconciliation procedures, DAS State Accounting Division (State Accounting) has identified a large unknown statewide variance between the State Treasurer's bank statements and the State's balances in the general ledger. This unknown variance indicates the bank records are short as compared to the accounting records. Some adjustments to the accounting records may be needed and may affect the fund balances of the Department. At this time, it has not been determined how or when adjustments to the accounting records might be made. State Accounting is unable to determine the affect of such adjustment, if any, on the Department's balances; however, State Accounting believes it will not have a material impact on the Department's operations.

STATE OF NEBRASKA  
Auditor of Public Accounts



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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM  
**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**

Nebraska Department of Environmental Quality  
Lincoln, Nebraska

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, 2006, and have issued our report thereon dated March 21, 2007. The Independent Auditors' 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.

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 an opinion 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 reportable 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 caused by error or fraud in amounts that would be material in relation to the financial statements being examined 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.

Compliance and Other Matters

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 or other matters that are required to be reported under *Government Auditing Standards*.

However, we noted an item that we have reported to management of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program in a separate letter dated March 21, 2007.

This report is intended solely for the information and use of the Program, the appropriate Federal and regulatory agencies. However, this report is a matter of public record and its distribution is not limited.

Pat Reding, CPA

Assistant Deputy Auditor

March 21, 2007

STATE OF NEBRASKA  
Auditor of Public Accounts



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NEBRASKA DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING FUND PROGRAM  
**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL  
OVER 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**

Nebraska Department of Environmental Quality  
Lincoln, Nebraska

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, 2006. 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/Cost 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.

Compliance

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.

In our opinion, 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, 2006.

#### Internal Control Over Compliance

The management of the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants. In planning and performing our audit, we considered the Nebraska Department of Environmental Quality - Clean Water State Revolving Fund Program's internal control over compliance with requirements that could have a direct and material effect in order to determine our auditing procedures for the purpose of expressing an opinion on compliance and to test and report on the internal control over compliance.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable 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 noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to the Federal program 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 compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the Program and the appropriate Federal and regulatory agencies. However, this report is a matter of public record and its distribution is not limited.

*Pat Reding, CPA*

Assistant Deputy Auditor

March 21, 2007