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STATE OF MISSISSIPPI  
DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING LOAN FUND

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Audited Financial Statements  
June 30, 2007

State of Mississippi  
Department of Environmental Quality  
Clean Water State Revolving Loan Fund

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## Independent Auditor's Report

Commission on Environmental Quality  
Mississippi Department of Environmental Quality

We have audited the accompanying financial statements of the State of Mississippi Department of Environmental Quality Clean Water State Revolving Loan Fund (the Fund) as of and for the year ended June 30, 2007, as listed in the table of contents. These financial statements are the responsibility of the Fund'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 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 Note 1, the financial statements referred to above are intended to present only the financial position and results of operations of the Clean Water State Revolving Loan Fund of the Mississippi Department of Environmental Quality, a department of the State of Mississippi. These statements are not intended to present the financial position and results of operations for the State of Mississippi or the Mississippi Department of Environmental Quality, of which the Clean Water State Revolving Loan Fund is a part.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Fund as of June 30, 2007, and the results of its operations 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 a report dated September 27, 2007, on our consideration of the State of Mississippi Department of Environmental Quality Clean Water State Revolving Loan Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Windham and Lacey, PLLC  
September 27, 2007

**STATE OF MISSISSIPPI  
DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING LOAN FUND  
BALANCE SHEET  
JUNE 30, 2007**

<b>ASSETS</b>	<u>June 30, 2007</u>	<u>June 30, 2006</u>
Equity in internal investment pool	\$ 40,777,175	72,480,961
Cash in transit		2,151
Repurchase agreements	493,080	
Receivables:		
Interest	3,069	
Due from other funds	7,772	
Due from other governments	331,409,550	280,367,901
Due from federal government	80,746	
<b>TOTAL ASSETS</b>	<u>\$ 372,771,392</u>	<u>352,851,013</u>
<b>LIABILITIES AND FUND BALANCE</b>		
<b>LIABILITIES:</b>		
Warrants payable	\$ 2,543,212	2,121,622
Funds held for others	7,772	
Due to other funds	96,899	\$100,628
Due to other governments	6,369,722	10,586,284
<b>TOTAL LIABILITIES</b>	<u>9,017,605</u>	<u>12,808,534</u>
<b>FUND BALANCE:</b>		
Reserved for long-term portion of due from other governments	315,841,260	268,750,700
Unreserved	47,912,527	71,291,780
<b>TOTAL FUND BALANCE</b>	<u>363,753,787</u>	<u>340,042,480</u>
<b>TOTAL LIABILITIES AND FUND BALANCE</b>	<u>\$ 372,771,392</u>	<u>352,851,014</u>

See accompanying Notes to Financial Statements.

**STATE OF MISSISSIPPI  
DEPARTMENT OF ENVIRONMENTAL QUALITY  
CLEAN WATER STATE REVOLVING LOAN FUND  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE  
YEAR ENDED JUNE 30, 2007**

	<u>June 30, 2007</u>	<u>June 30, 2006</u>
REVENUES:		
Interest on loans	\$ 4,710,783	5,379,658
Interest on investments	2,396,925	2,446,948
Federal programs	15,619,593	165,357
Bond proceeds	<u>2,013,000</u>	
TOTAL REVENUES	<u>24,740,301</u>	<u>7,991,963</u>
EXPENDITURES		
Bond issuance costs	<u>1,070</u>	<u>0</u>
EXCESS OF REVENUES OVER EXPENDITURES	<u>24,739,231</u>	<u>7,991,963</u>
OTHER FINANCING SOURCES (USES):		
Transfers in	348,841	490,997
Transfers out	<u>(1,376,765)</u>	<u>(198,436)</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>(1,027,924)</u>	<u>292,561</u>
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES AND OTHER FINANCING USES	23,711,307	8,284,524
FUND BALANCE:		
Beginning of Year	<u>340,042,480</u>	<u>331,757,956</u>
End of Year	<u>\$ 363,753,787</u>	<u>340,042,480</u>

See accompanying Notes to Financial Statements.



STATE OF MISSISSIPPI  
Department of Environmental Quality  
Clean Water State Revolving Loan Fund  
Notes to Financial Statements  
June 30, 2007

**1. ORGANIZATION AND NATURE OF OPERATIONS OF THE FUND.**

The Clean Water State Revolving Loan Fund (the Fund) of the Mississippi Department of Environmental Quality (MDEQ) was established pursuant to Title VI of the Federal Water Quality Act of 1987 (the Act). The Act established the State Revolving Fund (SRF) Program to replace the construction grants program and to provide loans at reduced interest rates to finance the construction of publicly owned water pollution control facilities, non-point source pollution control projects, and estuary management projects. Instead of making grants to subdivisions that pay for a portion of building wastewater treatment facilities, the Fund provides for low interest rate loans to finance the entire cost of qualified projects. The Fund provides a flexible financing source that can be used for a variety of pollution control projects, including non-point source pollution control projects, and developing estuary conservation and management projects. All loan repayments, including interest and principal, must remain in the Fund.

The Fund was funded by the U.S. Environmental Protection Agency (EPA) by a series of grants starting in 1989. In order to receive a grant, states are required to provide an additional 20 percent of the federal capitalization grant as matching funds. As of June 30, 2007, Congress authorized the EPA to award \$233,442,613 in capitalization grants to the State of Mississippi (the State). The State is required to contribute \$46,688,523, in matching funds. In prior years the State was awarded hardship grants totaling \$1,045,000, which required matching contributions of \$52,250. Hardship grants are maintained in the same fund with capitalization grants, with subsidiary records to account for grant balances and transactions separately. Because all hardship grants have been obligated and paid out to grant recipients, there were no hardship grant payments made for the year ended June 30, 2007.

The Fund is administered by the Commission on Environmental Quality (the Commission) acting through the Construction Branch (the Branch) of the Surface Water Division of the Office of Pollution Control of MDEQ. MDEQ's primary activities include the making of loans for water pollution control facilities and the management and coordination of the Fund. The Commission consists of seven members, all of which are appointed by the Governor.

The Fund does not have any full-time employees. The Fund is administered by employees of the Branch. All employee and related costs are recorded in MDEQ's Office of Pollution Control Operating Fund. Operating costs are reimbursed from the avails of a 5% administrative fee collected from each loan recipient (see Note 6).

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES.**

The Fund is included in the State's basic financial statements as a general fund of the State of Mississippi.

***Basis of Accounting***

The Fund presents its financial statements as a general fund and uses the modified accrual basis of accounting. Revenues are recognized when both "measurable and available". Measurable means the amount can be determined. Available means amounts collectible within the current period or soon enough thereafter to pay current liabilities. Expenditures are recorded when the related liability is incurred. The Fund applies all relevant Governmental Accounting Standards Board (GASB) pronouncements, as well as applicable statements issued by the Financial Accounting Standards Board.

***Equity in Internal Investment Pool***

Monies of the Fund deposited with the State Treasurer's Office internal investment pool are considered cash and cash equivalents. According to state law, the Treasurer is responsible for maintaining the cash balances and investing excess cash of the Fund, as discussed in Note 3. Therefore, management of the Fund does not have any control over the investment of excess cash.

STATE OF MISSISSIPPI  
Department of Environmental Quality  
Clean Water State Revolving Loan Fund  
Notes to Financial Statements  
June 30, 2007

***Due from Other Governments***

The State operates the Fund as a direct loan program, whereby loans made to political subdivisions are funded by the federal capitalization grant, the state matching amount, loan repayments and interest earnings. Loan funds are disbursed to the political subdivision as they expend funds for the purposes of the loan and request reimbursement from the Fund. Interest is calculated from original contract completion date, and, after the final disbursement has been made, the principal amount identified in the loan agreement is adjusted for the actual amounts disbursed plus interest accrued during the period between the original construction contract completion date and the initiation of the repayment process.

***Fund Balance***

The unreserved fund balances represent the amount available for funding future operations. The reserved fund balances represent the amount that has been legally restricted to a specific purpose or that is not available for appropriation or expenditure. The Fund had the following reserved fund balance at year end:

Reserved for long-term portion of due from other governments - An account used to indicate the noncurrent portions of loans receivable that do not represent available expendable resources.

***Comparative Data***

Comparative prior year totals have been presented in the accompanying financial statements to provide an understanding of the change in the Fund's financial condition and operations and are not intended to be a complete presentation of the prior year financial statements in accordance with accounting principles generally accepted in the United States of America.

***Budget Information***

Under the Constitution of the State of Mississippi, money may only be drawn from the Treasury by a legal appropriation. The Fund operations are included in MDEQ's annual budget.

**3. EQUITY IN INTERNAL INVESTMENT POOL.**

All monies of the Fund are deposited with the State Treasurer and are considered to be cash and cash equivalents. The Treasurer is responsible for maintaining the cash balances in accordance with state laws, and excess cash is invested in the State's cash and short-term investment pool. Details of the investments of the internal investment pool for state agencies can be obtained from the State Treasurer. As of June 30, 2007, the State's total pooled deposits and investments for state agencies were approximately \$2.9 billion, and the average remaining life of the securities invested was 2.77 years. The earnings for the total pooled investments for the year ended June 30, 2007 were approximately \$88.3 million.

Equity in internal investment pool is cash equity with the Treasurer and consists of pooled deposits and investments carried at cost, which approximates fair value. At June 30, 2007, the Fund had approximately \$40.7 million in the Treasurer's internal investment pool. The total deposits and investments of the internal investment pool are categorized according to credit risk in the State of Mississippi's Comprehensive Annual Financial Report. However, the Fund's portion of the internal investment pool cannot be individually categorized because the deposits and investments are pooled with other state agencies.

STATE OF MISSISSIPPI  
 Department of Environmental Quality  
 Clean Water State Revolving Loan Fund  
 Notes to Financial Statements  
 June 30, 2007

**4. DUE FROM OTHER GOVERNMENTS AND CREDIT RISK.**

The Fund makes loans to qualified public subdivisions for projects that meet the eligibility requirements of the Act. Loans are financed by capitalization grants, state match, loan repayments and interest earnings. Interest rates on loans vary between 1.75% and 4.5%, and are generally repaid over 20 years starting within one year after the project is completed. Details of loans receivable as of June 30, 2007, are discussed below:

In the event of a default on a loan obligation by a public entity, MDEQ has certain legal remedies available that provide for ultimate collection of amounts due.

***Loans by Category***

Due from other governments at June 30, 2007, is as follows:

	Loans Authorized	Authorized Amount Remaining	Cumulative Repayments	Balance
Completed projects	\$ 347,669,413		107,392,353	240,277,060
Projects in progress	<u>129,842,182</u>	<u>38,709,692</u>		<u>91,132,490</u>
Totals	<u>\$ 477,511,595</u>	<u>38,709,692</u>	<u>107,392,353</u>	331,409,550
Less: Amount due within one year on completed projects				<u>(15,568,290)</u>
Due from other governments, long-term				<u>\$ 315,841,260</u>

Loans mature at various intervals through June 30, 2027. The scheduled principal payments on loans maturing in subsequent years are as follows:

<u>Year Ending June 30</u>	<u>Amount</u>
2008	\$ 15,568,290
2009	16,489,851
2010	18,230,034
2011	19,065,918
2012	18,480,472
Thereafter	<u>243,574,985</u>
Totals	<u>\$ 331,409,550</u>

STATE OF MISSISSIPPI  
Department of Environmental Quality  
Clean Water State Revolving Loan Fund  
Notes to Financial Statements  
June 30, 2007

***Major Loans to Political Subdivisions***

As of June 30, 2007, the Fund had made loans to 26 local agencies that, in the aggregate, exceeded \$5,000,000 for each local agency. The outstanding balances of these loans represent approximately 52% of the total loans receivable, as follows:

Local Agency	Authorized Loan Amount	Loan Receivable Balance at June 30, 2007
City of Brandon	\$ 7,059,663	5,379,974
City of Cleveland	6,343,960	5,813,686
City of Clinton	16,388,095	13,244,359
City of Columbus	16,403,709	11,756,002
City of Corinth	17,132,428	11,245,042
DeSoto County Regional WWA	31,557,619	26,591,671
City of Forest	5,065,949	1,959,495
City of Greenville	11,773,543	7,489,966
City of Greenwood	17,082,554	13,149,176
City of Gulfport	45,291,179	34,299,838
Hancock County Water and Sewer District	9,270,921	7,891,106
Harrison County Water Works Management District	20,051,748	13,889,913
City of Hattiesburg	5,650,110	3,458,354
Horn Lake Creek Basin Interceptor Sewer District	7,840,454	3,473,776
City of Jackson	30,214,536	19,422,117
City of Magnolia	6,627,201	4,136,544
City of Laurel	11,316,308	7,643,434
Mississippi Gulf Coast Regional WWA	13,644,626	450,510
City of Morton	5,761,042	3,257,659
City of Oxford	10,283,744	1,263,156
City of Pascagoula	6,324,921	2,712,813
City of Pontotoc	6,342,006	5,359,626
Southern Regional Waste Water	11,323,026	10,114,104
City of Tupelo	30,823,858	29,324,123
City of Vicksburg	10,038,672	5,858,636
West Jackson County Utility	5,864,635	3,613,475
Totals	\$ 365,476,507	252,798,554

The authorized loan amount includes both completed projects and projects in progress. As of June 30, 2007, cumulative principal repayments on completed projects from the above local agencies total \$74,019,485 and amounts remaining to be disbursed on projects in progress total \$41,860,157.

STATE OF MISSISSIPPI  
Department of Environmental Quality  
Clean Water State Revolving Loan Fund  
Notes to Financial Statements  
June 30, 2007

**5. GRANT AWARDS.**

The Fund is funded by grants from the EPA authorized by Title VI of the Act, matching funds from the State, loan repayments and interest earnings. All funds drawn are recorded as grant awards from the EPA. As of June 30, 2007, the EPA has awarded capitalization and hardship grants of \$234,487,613 to the State, of which \$231,528,083 has been drawn for loans and administrative expenses.

The following summarizes the capitalization grants awarded, amounts drawn on each grant and balances available for future loans:

Year	Grant Amount	Draws Through 6/30/2006	2007 Draws	Draws Through 6/30/2007	Available 6/30/2007
1989	\$ 15,254,024	15,254,024		15,254,024	
1990	15,780,824	15,780,824		15,780,824	
1991	19,512,358	19,512,358		19,512,358	
1992	17,505,576	17,505,576		17,505,576	
1993	17,316,882	17,316,882		17,316,882	
1994	10,744,965	10,744,965		10,744,965	
1995	11,583,952	11,583,952		11,583,952	
1996	18,185,133	18,185,133		18,185,133	
1997	5,572,572	5,572,572		5,572,572	
1998	12,316,944	12,316,944		12,316,944	
1998					
Hardship	1,045,000	1,045,000		1,045,000	
1999	12,133,044	12,133,044		12,133,044	
2000	12,091,860	12,091,860		12,091,860	
2001	11,984,346	11,984,346		11,984,346	
2002	12,011,076	12,011,076		12,011,076	
2003	11,932,965	11,932,965		11,932,965	
2004	11,940,192	11,017,715	922,477	11,940,192	
2005	9,706,600		9,699,729	9,699,729	6,871
2006	7,869,300		4,916,641	4,916,641	2,952,659
Totals	\$ 234,487,613	215,989,236	15,538,847	231,528,083	2,959,530
Receivable, June 30, 2006					
Receivable, June 30, 2007			80,746		(80,746)
Grant revenues, modified accrual basis		\$ 15,619,593			
Amount available, modified accrual basis				\$ 2,878,784	

STATE OF MISSISSIPPI  
Department of Environmental Quality  
Clean Water State Revolving Loan Fund  
Notes to Financial Statements  
June 30, 2007

As of June 30, 2006 and 2007, state matching contributions were as follows:

	Contributions through 6/30/2006	Fiscal Year 2007 Contributions	Contributions through 6/30/2007
State of Mississippi	\$ 43,051,395	3,108,516	46,159,911

**6. ADMINISTRATIVE FEES/COSTS.**

In connection with issuing loans to political subdivisions, certain administrative and processing functions are performed by the Construction Branch (the Branch) of the Surface Water Division of the Office of Pollution Control of MDEQ, as discussed in Note 1. To help fund the cost of such functions and MDEQ's indirect costs, a 5% administrative fee is collected from each loan recipient. Until fiscal year 1999, administrative fees were added to the loan principal amount to be repaid by the loan recipient.

However, for all loans made after October 1, 1998, the 5% administrative fee is no longer added to the loan principal to be repaid by the loan recipient. Instead, it is collected through the loan repayment stream. Beginning with the initiation of the repayment process and until such time the total administrative fee is collected, the interest portion of each loan repayment is used to satisfy collection of the administrative fee in lieu of the interest portion. The administrative fees and costs related thereto are recognized on the financial statements of MDEQ's Office of Pollution Control SRF Administrative Fee Fund 3588.

Administrative fees collected for the fiscal year ended June 30, 2007, totaled \$1,262,391. During that period, \$1,235,497 was expended from available administrative fee funds for administrative costs of the Fund. \$1,025,513 was drawn in fiscal year 2007 from the federal government for administrative expenses.

**7. CONTINGENCIES.**

The Fund is exposed to various risks of loss related to torts, theft of assets, errors or omissions, injuries to state employees while performing Fund business, or acts of God. MDEQ maintains insurance for some risks of loss, which is included in the administrative fees charged to the Fund. Risks of loss related to torts are administered by the Mississippi Tort Claims Board. Since its inception in 1989, there have not been any claims against the Fund.

**8. HURRICANE KATRINA LOAN FORBEARANCE**

On August 29, 2005, Hurricane Katrina swept through Mississippi causing widespread destruction, including that to water and sewer operations. Some loan fund projects in progress, as well as, future projects included in the Intended Use Plan were impacted. The current portion of Due from Other Governments and loan repayments due for future years may be delayed if sales tax diversions of impacted areas are placed in abeyance for a period of time or if water and sewer collections from impacted areas are insufficient to support loan repayment schedules. The Commission has granted forbearance of loan repayment for up to three years and four months to those water systems that have been impacted. In addition to a forbearance of loan repayments, the Commission will not accrue interest on those loans during the forbearance period. For the fiscal year ended June 30, 2007, forbearance has reduced the amount of revenue to the Fund for interest on loans by \$1,126,912. Federal law requires repayment of loans over a 20 year period and as of the date of this report, Congress has not extended this repayment period. At the end of the forbearance period the loans will be restructured. The ability of these entities to repay these loans within the allotted period is uncertain at this time; thus, the future economic impact is undeterminable.

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**Independent Auditor's Report on Internal Control  
Over Financial Reporting and on  
Compliance and Other Matters  
Based on an Audit of the Financial Statements  
Performed In Accordance with  
*Government Auditing Standards***

Commission on Environmental Quality  
Mississippi Department of Environmental Quality

We have audited the financial statements of the State of Mississippi Department of Environmental Quality Clean Water State Revolving Loan Fund as of and for the year ended June 30, 2007, and have issued our report thereon dated September 27, 2007. 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 Mississippi Department of Environmental Quality Clean Water State Revolving Loan Fund'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 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. 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 Mississippi Department of Environmental Quality Clean Water State Revolving Loan Fund's 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 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*.

This report is intended solely for the information and use of management of the Clean Water State Revolving Loan Fund, the Governor, Members of the Legislature and the United States Environmental Protection Agency and is not intended to be and should not be used by anyone other than the specified parties.

Windham and Lacey, PLLC  
September 27, 2007



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**Independent Auditor's Report on Compliance  
with the Requirements Applicable to the  
Environmental Protection Agency's  
Capitalization Grants for Clean Water  
State Revolving Funds  
in Accordance with  
*Government Auditing Standards***

Commission on Environmental Quality  
Mississippi Department of Environmental Quality

We have audited the financial statements of the State of Mississippi Department of Environmental Quality Clean Water State Revolving Loan Fund (the Fund) as of and for the year ended June 30, 2007, and have issued our report thereon dated September 27, 2007.

We have also audited the Fund's compliance with requirements governing:

- Activities allowed or unallowed,
- Allowable costs/cost principles,
- Cash management,
- State matching,
- Period of availability of federal funds and binding commitments,
- Procurement, suspension and debarment,
- Program income,
- Reporting,
- Subrecipient monitoring, and
- Special tests and provisions

that are applicable to the Clean Water State Revolving Loan Fund Program for the year ended June 30, 2007. The management of the Clean Water State Revolving Loan Fund Program is responsible for the Fund's compliance with those requirements. Our responsibility is to express an opinion on those requirements based on our audit.

We conducted our audit of compliance with those requirements in accordance with auditing standards generally accepted in the United States of America and *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 material noncompliance with the requirements referred to above occurred. An audit includes examining, on a test basis, evidence about the Fund'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 Fund's compliance with those requirements.

In our opinion, the Fund complied, in all material respects, with the requirements governing activities allowed or unallowed; allowable costs/cost principles; cash management; state matching; period of availability of federal funds and binding commitments; procurement suspension and debarment; program income; reporting; subrecipient monitoring; and special tests and provisions that are applicable to the Clean Water State Revolving Loan Fund Program for the year ended June 30, 2007.

This report is intended for the information and use of management of the Clean Water State Revolving Loan Fund, the Governor, Members of the Legislature and the United States Environmental Protection Agency and is not intended to be and should not be used by anyone other than the specified parties.

Windham and Lacey, PLLC  
September 27, 2007