

MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA



FINANCIAL STATEMENT AUDIT
ISSUED JULY 6, 2005

**LEGISLATIVE AUDITOR
1600 NORTH THIRD STREET
POST OFFICE BOX 94397
BATON ROUGE, LOUISIANA 70804-9397**

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STEVE J. THERIOT, CPA
LEGISLATIVE AUDITOR

OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

1600 NORTH THIRD STREET
POST OFFICE BOX 94397
TELEPHONE: (225) 339-3800
FACSIMILE: (225) 339-3870

June 16, 2005

Independent Auditor's Report
on the Financial Statements

MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA
Baton Rouge, Louisiana

We have audited the accompanying financial statements of the Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund, as of and for the year ended June 30, 2004, as listed in the table of contents. These financial statements are the responsibility of management of the Municipal Facilities Revolving Loan Fund Program. 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 that our audit provides a reasonable basis for our opinion.

As discussed in note 1, the accompanying financial statements present only the Municipal Facilities Revolving Loan Fund, and do not purport to, and do not, present fairly the financial position of the State of Louisiana or the Louisiana Department of Environmental Quality and the respective changes in financial position, including cash flows, in conformity with accounting principles generally accepted in the United States of America.

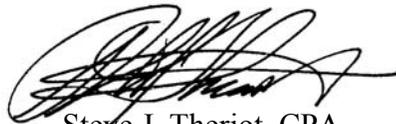
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund as of June 30, 2004, and its changes in financial position, including cash flows, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

MUNICIPAL FACILITIES REVOLVING LOAN FUND

In accordance with *Government Auditing Standards*, we have also issued a report dated June 16, 2005, on our consideration of the Municipal Facilities Revolving Loan Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in assessing the results of our audit.

In addition, we have issued a report dated June 16, 2005, on our consideration of the Municipal Facilities Revolving Loan Fund's internal control over compliance with certain laws and regulations, and our tests of its compliance with those laws and regulations, in accordance with the *Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*.

Respectfully submitted,



Steve J. Theriot, CPA
Legislative Auditor

AOE:BQD:THC:dl

DEQMFRLF04

**MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA
PROPRIETARY FUND - ENTERPRISE FUND**

Statement of Net Assets, June 30, 2004

ASSETS

Current assets:

Cash in state treasury (note 2)	\$110,060,631
Receivables - due from others (note 3)	1,305,161
Current loans receivable (note 4)	8,972,938
Total current assets	<u>120,338,730</u>

Noncurrent assets - loans receivable (note 4)	<u>180,379,522</u>
Total assets	<u><u>300,718,252</u></u>

LIABILITIES

Current liabilities - accounts payable and accrued expenses	<u>79,377</u>
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NET ASSETS - unrestricted	<u><u>\$300,638,875</u></u>
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The accompanying notes are an integral part of this statement.

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**MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA
PROPRIETARY FUND - ENTERPRISE FUND**

**Statement of Revenues, Expenses, and
Changes in Fund Net Assets
For the Fiscal Year Ended June 30, 2004**

OPERATING REVENUES	
Interest earned on loans receivable	\$6,266,711
Interest earned on cash in state treasury	1,047,824
Total operating revenues	<u>7,314,535</u>
OPERATING EXPENSES	
Administrative expenses (note 8)	<u>896,713</u>
OPERATING INCOME	6,417,822
Capital contributions (note 7)	<u>20,810,894</u>
CHANGE IN NET ASSETS	27,228,716
NET ASSETS - BEGINNING OF YEAR	<u>273,410,158</u>
NET ASSETS - END OF YEAR	<u><u>\$300,638,874</u></u>

The accompanying notes are an integral part of this statement.

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**MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA
PROPRIETARY FUND - ENTERPRISE FUND**

**Statement of Cash Flows
For the Fiscal Year Ended June 30, 2004**

CASH FLOWS FROM OPERATING ACTIVITIES:

Cash received from borrowers	\$67,789,334
Cash received from interest on cash in state treasury	982,890
Cash payments for administrative expenses	(878,535)
Cash payments to borrowers	(38,553,658)
Net cash provided by operating activities	29,340,031

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:

Capital contributions	20,807,364
Fees paid on bonds	(13,945)
Net cash provided by noncapital financing activities	20,793,419

Net increase in cash 50,133,450

Cash at beginning of the year 59,927,181

Cash at end of the year \$110,060,631

**RECONCILIATION OF OPERATING INCOME TO
NET CASH PROVIDED BY OPERATING ACTIVITIES:**

Operating income	\$6,417,822
Adjustments to reconcile operating income to net cash used by operating activities:	
Fees paid on bonds	13,945
Changes in assets and liabilities:	
Decrease in loans receivable	22,467,688
Decrease in due from others and accounts receivable	436,342
Increase in accounts payable and accrued expenses	4,234
	4,234

NET CASH PROVIDED BY OPERATING ACTIVITIES \$29,340,031

The accompanying notes are an integral part of this statement.

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INTRODUCTION

The Louisiana Department of Environmental Quality (DEQ) is a department of the State of Louisiana. DEQ was created in accordance with Louisiana Revised Statute (R.S.) 30:2011 as a part of the executive branch of government. DEQ is charged with environmental protection within the State of Louisiana.

The Municipal Facilities Revolving Loan Fund (MFRLF) program was established pursuant to Title VI of the Clean Water Act, as amended in 1987 (the Act). The MFRLF program presently operates under R.S. 30:2078-2089. These statutes establish a state revolving loan fund capitalized by federal grants (Capitalization Grants for Clean Water State Revolving Funds, CFDA 66.458), by state funds when required or available, and by any other funds generated by the operation of the clean water revolving loan fund. DEQ is authorized to engage in activities regarding the sums on deposit in, credited to, or to be received by the state revolving loan fund. The Financial Services, Environmental Technology, and Environmental Evaluation Divisions within DEQ are responsible for the operations of the MFRLF Program in the State of Louisiana. These divisions within DEQ provide assistance to municipalities in the development, financing, and implementation of wastewater treatment management plans and plants. Engineering oversight, design review and inspection services are provided by the Environmental Technology Division; environmental assessment services are provided by the Environmental Evaluation Division; and grant management, program administration and financial services are provided by the Financial Services Division on eligible wastewater treatment projects. All efforts are directed toward improving water quality by assisting communities in providing wastewater treatment processes that meet established effluent limits and achieve the goals of the Act.

The MFRLF does not have any full-time employees. However, time spent on the MFRLF Program by employees of DEQ is captured and the MFRLF subsequently reimburses DEQ for salaries and benefits as well as other operating expenses of the fund.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. BASIS OF PRESENTATION

The accompanying financial statements have been prepared on the full accrual basis in accordance with accounting principles generally accepted in the United States of America as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting principles and reporting standards. These principles are found in the *Codification of Governmental Accounting and Financial Reporting Standards*, published by the GASB. Management of the fund applies all GASB pronouncements as well as Financial Accounting Standards Board (FASB) statements and interpretations issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. Management has elected to follow GASB statements issued after November 30, 1989, rather than the FASB statements.

B. REPORTING ENTITY

GASB Codification Section 2100 establishes criteria for determining the governmental reporting entity and has defined the governmental reporting entity to be the State of Louisiana. The accompanying financial statements represent activity of a fund of the State of Louisiana that is administered by DEQ, a department within state government. The MFRLF is part of the primary government of the State of Louisiana.

Annually, the State of Louisiana issues a comprehensive annual financial report, which includes the activity contained in the accompanying financial statements. Those basic financial statements are audited by the Louisiana Legislative Auditor.

C. FUND ACCOUNTING

For the purposes of this report, the MFRLF uses a single proprietary (enterprise) fund. Proprietary funds are used to account for operations that are (a) financed and operated in a manner similar to private business enterprises where the intent of the governing body is that costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or (b) where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes.

D. BASIS OF ACCOUNTING

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made, regardless of the measurement focus applied. The transactions of the MFRLF are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and liabilities associated with the operations are included on the Statement of Net Assets.

The MFRLF uses the accrual basis of accounting. Revenues are recognized in the accounting period when they are earned and expenses are recognized when the related liability is incurred.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and/or producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the MFRLF are federal funds and interest earnings. Operating expenses include the administrative expenses of the program and bond issuance and related costs. Any revenues and expenses not meeting this definition would be reported as nonoperating revenues and expenses.

E. BUDGETS AND BUDGETARY ACCOUNTING

The MFRLF is budgeted annually by the Louisiana Legislature through the Ancillary Appropriations Act. The Ancillary Appropriations Act (Act 44 of the 2003 Regular Session as amended) authorized expenditures of \$45,000,000 for the loan program for fiscal year 2003-2004 and allows the fund to retain resources to fund future loans and eligible program activities. Because the fund is an enterprise fund, a budgetary comparison is neither required nor presented in the financial statements.

F. LOANS RECEIVABLE

The MFRLF is operated as a direct loan program. The program provides loans and other financial assistance to municipalities for the purpose of planning, constructing publicly owned treatment works, implementing nonpoint source pollution management programs, and developing and implementing estuary conservation and management plans.

The program lends federal and state monies directly to municipalities. The federal share is 80% and requires a state matching share of 20%. Recycling of principal and interest repayments from borrowing municipalities allows the program to operate in perpetuity thereby benefiting other municipalities wishing to borrow in the future. Borrowers pay principal and interest directly to the loan program, and all monies are deposited directly to the program. Principal repayments can only be used to make additional loans to municipalities. Interest earnings on investments and loans can also be used to make additional loans. In addition, with Environmental Protection Agency (EPA) approval, interest earnings on investments and loans are used to pay off revenue bonds sold to capitalize the program by providing state matching funds.

The loans made by the MFRLF must be made at or below market interest rate with a repayment period not exceeding 20 years plus an interim construction-financing period. The current loan rate is 3.45% interest and .5% administrative fee for new sewer construction/sewer system rehabilitation projects. Several loans have been made at higher interest rates and the program has the ability to change its interest rates as necessary.

As evidence of its obligations to pay principal and interest on the loans, each borrower must establish a dedicated source of revenue for repayment of the loan [33 USC 1383(d)(1)(C)]. For substantially all of these loans, the loan recipient issues bonds that are purchased by DEQ, as administrator of the MFRLF, to secure the repayment of the principal loaned. Principal and interest on the bonds are paid to the MFRLF and upon repayment of the loan, the bonds are returned to the loan recipient. Minimum required coverage ratios are established depending on the nature of the bonded indebtedness issued by the loan recipient as follows:

For limited tax bonds, the principal and interest due in any year on the amount borrowed shall not exceed 75% of the revenues estimated to be received from the levy of the pledged millage in the year in which the indebtedness is issued (R.S. 39:742.2).

For sales tax bonds, the total amount of principal and interest falling due in any year, together with principal and interest falling due in such year on any previously issued sales tax bonds, shall never exceed 75% of the amount of sales tax revenues estimated by the governing authority of the issue to be received by it in the calendar year in which the bonds are issued (R.S. 39:698.4).

For revenue bonds, the requirements for coverage are established contractually in the loan documents (R.S. 39:1019). Expected coverage ratios might range from 110% to 130% or more. The MFRLF goal for collections of the dedicated revenues for repayment of the loan secured by revenue bonds is 125%; however, many factors can create deviation from this goal. It is customary to use the same minimum required coverage ratio as was previously established for outstanding debt of the loan recipient.

For general obligation bonds, the requirements for coverage are statutorily set. The governing authority of the issuer is required to impose and collect annually, in excess of all other taxes, a tax on all property subject to taxation by the issuer sufficient in amount to pay the interest and the principal falling due each year, or such amount as may be required for any sinking fund necessary to retire said bonds at maturity (R.S. 39:569). Typically, the bond millage is adjusted each year so as to generate enough revenues to pay debt service in the ensuing calendar year. No coverage requirements or debt service reserves exist, because the tax can be adjusted each year *without any limitation whatsoever* to collect the appropriate amount each year.

In the case of sales tax bonds and revenue bonds, each loan recipient is also required to set up a debt service reserve fund equal to 10% of the loan amount or one year's principal and interest for the purpose of paying principal and interest should the dedicated revenues be insufficient for that purpose. The requirement to maintain a debt service reserve fund is not statutorily required, but is usual and customary for these kinds of indebtedness.

Because of the reserve requirements and the absence of any delinquent loans, there is no provision for uncollectible amounts.

G. NET ASSETS

Net assets comprise the various net earnings from operations, nonoperating revenues, and contributions of capital. Net assets generally are classified in the following components:

Invested in capital assets, net of related debt consists of all capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

Restricted net assets consist of net assets subject to external constraints placed on net asset use by creditors, grantors, contributors or law or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of all other net assets that are not included in the other categories previously mentioned.

H. CAPITAL CONTRIBUTIONS

The funds drawn for loans from the EPA capitalization grants authorized by Title VI of the Clean Water Act, as amended in 1987, are recorded as capital contributions.

I. CAPITAL ASSETS

The MFRLF has no capital assets or long-term obligations at June 30, 2004.

J. COMPENSATED ABSENCES

The MFRLF has no full-time employees. The fund pays a portion of the salary of various employees of the Department of Environmental Quality for administrative services. Therefore, no compensated absences, pension benefits, or postretirement benefits are provided by the fund.

K. ESTIMATES

The preparation of financial statements requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

2. CASH

As reflected on Statement A, the MFRLF has cash totaling \$110,060,631 at June 30, 2004. All monies of the fund are deposited with the State Treasurer's Office. Cash balances are held and controlled by the state treasurer and are secured from risk by the state treasurer through separate custodial agreements, and the risk disclosures required by accounting principles generally accepted in the United States are included within the State of Louisiana's financial statements.

MUNICIPAL FACILITIES REVOLVING LOAN FUND

3. DUE FROM OTHERS

As shown on Statement A, the MFRLF has a total due from others of \$1,305,161. This total is comprised of the following:

Due from state treasury	\$122,201
Due from federal government	66,145
Due from municipalities	<u>1,116,815</u>
Total due from others	<u><u>\$1,305,161</u></u>

The \$1,116,815 due from municipalities is interest due on loans.

4. LOANS RECEIVABLE

The MFRLF makes loans to qualified political subdivisions of the State of Louisiana for projects that meet the eligibility requirements of the program. Loans are financed by capitalization grants, state match, and revolving funds. Effective interest rates on loans vary between 2.45% and 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, 2004, are as follows:

Projects in progress	\$86,596,765
Completed projects	<u>102,755,695</u>
Total loans receivable	<u><u>\$189,352,460</u></u>

Loans mature at various intervals through July 1, 2025. The scheduled principal payments on loans maturing in subsequent years are as follows:

	<u>Projects in Progress</u>	<u>Completed Projects</u>	<u>Total</u>
Year ending June 30:			
2005	\$2,999,260	\$5,973,678	\$8,972,938
2006	3,473,000	6,152,525	9,625,525
2007	3,594,000	6,346,516	9,940,516
2008	3,725,000	6,549,653	10,274,653
2009	3,859,000	6,759,942	10,618,942
Thereafter	<u>68,946,505</u>	<u>70,973,381</u>	<u>139,919,886</u>
Total	<u><u>\$86,596,765</u></u>	<u><u>\$102,755,695</u></u>	<u><u>\$189,352,460</u></u>

Encumbered Balances

Over 43% of cash and undrawn capitalization grants are encumbered as follows:

Funds Encumbered

1. Cash and cash equivalents	\$110,060,631
2. Undrawn capitalization grants - 2003 grant	10,504,593
3. Total cash and undrawn grants	\$120,565,224
4. Loan in progress - encumbered	52,671,726
5. Loans (4) as percentage of total (3)	43.69%

The Loan in Progress - Encumbered represents the projects that are under construction and have only drawn a portion of the total approved loan amount. This figure consists of the total approved principal less the principal loaned to date.

Loans to Local Governments

As of June 30, 2004, the MFRLF had made loans to 21 municipalities that, in aggregate, exceeded or equaled \$4.5 million for each municipality. The outstanding balances of these loans represent approximately 90% of the total loans receivable as follows:

<u>Local Government</u>	<u>Authorized Loan Amount</u>	<u>Balance on Loans Outstanding</u>
Shreveport	\$76,000,000	\$17,881,013
St. Charles Parish	47,300,000	16,315,000
Monroe	37,000,000	30,749,646
Natchitoches	19,169,136	3,972,869
Lafayette	18,113,260	13,173,260
Kenner	12,890,678	8,550,000
Bogalusa	12,499,105	9,959,105
Opelousas	11,897,396	9,286,646
New Iberia	10,000,000	7,238,134
Bossier City	9,379,130	7,264,269
Slidell	7,998,177	3,020,937
Bastrop	7,500,000	5,010,000
Gonzales	7,294,064	5,149,064
Crowley	7,500,000	5,059,864
Walker	6,900,000	6,220,932
Jennings	6,500,000	4,390,000
Rayne	6,450,000	4,615,000
Springhill	6,279,304	4,241,000
Caddo-Bossier Port Commission	6,250,329	4,180,000
Leesville	4,710,000	3,040,000
Ruston	4,637,282	870,000
Total	\$326,267,861	\$170,186,739

5. REIMBURSEMENTS DUE TO MUNICIPALITIES FOR CONSTRUCTION

At June 30, 2004, no approved loan disbursement requests are in process.

6. LONG-TERM OBLIGATIONS

The MFRLF is allowed by statute to incur indebtedness but not allowed to issue bonds directly. To provide state matching funds when direct cash appropriations were not available, DEQ received approval from the EPA to borrow matching funds. The secretary of DEQ, through a Resolution by Executive Order pursuant to R.S. 30:2078 *et seq.*, was authorized, for state matching purposes, to borrow through the issuance of the department's note to the Louisiana Public Facilities Authority (LPFA), a conduit issuer of serial bonds for the department and the state.

The first serial bond issue was called Louisiana Public Facilities Authority Taxable Revenue Bonds (MFRLF Match Project) Series 1995. This indebtedness was secured solely from the pledge of a portion of the revenues received by the department from loans made by the program. The LPFA is a public trust and public corporation organized and existing for the benefit of the State of Louisiana. In accordance with the \$15,000,000 Loan Agreement between the LPFA and the department and in accordance with the \$15,000,000 Indenture of Trust between the LPFA and First National Bank of Commerce, the trustee, the LPFA issued serial bonds for \$15,000,000 and was repaid the \$15,000,000 by June 30, 1999. As of June 30, 2004, a total of \$14,654,221 had been generated for matching fund purposes by the issuance of these serial bonds.

The second serial bond titled Louisiana Public Facilities Authority Revenue Bonds (MFRLF Match Project) Series 2001 was issued during the fiscal year ending June 30, 2002. The Loan Agreement between the LPFA and DEQ was for a total of \$12,000,000 of which \$3,000,000 was issued during the fiscal year ending June 30, 2002. An additional \$6,000,000 was issued during the fiscal year ending June 30, 2003. No bonds were issued during the fiscal year ending June 30, 2004. The \$12,000,000 Indenture of Trust was issued between the LPFA and Hancock Bank of Louisiana. As of June 30, 2004, a total of \$8,847,241 was generated for matching fund purposes by the issuance of these serial bonds. Additional issuance from this series may be issued as needed for future state matching purposes. No liability for these bonds exists at June 30, 2004.

7. CAPITAL CONTRIBUTIONS, MATCHING, AND NET ASSETS

The MFRLF has been awarded 15 federal grants from the EPA. These grants are available through the EPA's Automated Clearing House Payment System (ACH) and the Automated Standard Application for Payments (ASAP). These grants are authorized by Title VI of the Clean Water Act, as amended in 1987 and require matching funds from the state. As of June 30, 2004, the EPA has awarded grants of \$234,933,068 to the state, of which \$224,428,475 has been drawn for loans and administrative expenses. The state has provided matching funds of

NOTES TO THE FINANCIAL STATEMENTS

\$50,255,048. The following summarizes the grants awarded, amounts drawn on each grant as of June 30, 2004, and balances available for future loans:

<u>Year</u>	<u>Grant Amount</u>	<u>Cumulative Dollars Drawn as of June 30, 2003</u>	<u>Current Fiscal Year Draws</u>	<u>Cumulative Dollars Drawn as of June 30, 2004</u>	<u>Remaining Grant Dollars Available as of June 30, 2004</u>
1988	\$12,000,000	\$12,000,000		\$12,000,000	
1989	10,368,765	10,368,765		10,368,765	
1990	10,725,264	10,725,264		10,725,264	
1991	22,560,714	22,560,714		22,560,714	
1992	21,359,349	21,359,349		21,359,349	
1993	21,129,174	21,129,174		21,129,174	
1994	13,110,372	13,110,372		13,110,372	
1995	13,540,230	13,540,230		13,540,230	
1996	22,179,267	22,179,267		22,179,267	
1997	6,820,400	6,820,400		6,820,400	
1998	22,190,138	22,190,138		22,190,138	
1999	14,804,064	14,804,064		14,804,064	
2000	14,753,871	12,829,844	\$1,924,027	14,753,871	
2001	14,736,260		14,736,260	14,736,260	
2003	14,655,200		4,150,607	4,150,607	\$10,504,593
Total	<u>\$234,933,068</u>	<u>\$203,617,581</u>	<u>\$20,810,894</u>	<u>\$224,428,475</u>	<u>\$10,504,593</u>

The state has provided its required matching share of federal grant awards through General Fund and state capital outlay appropriations totaling \$23,753,586. Tobacco Settlement monies of \$3,000,000 were deposited in the fund in the 2000 fiscal year. In addition, part of the required matching share has been provided through the issuance of Revenue Match Bonds secured by revenue of the fund. Beginning in fiscal year 1995, revenue bonds of \$15,000,000 were authorized. In fiscal year 2002, another \$12,000,000 in revenue match bonds were authorized. As of June 30, 2004, bonds totaling \$24,000,000 have been issued and repaid resulting in net proceeds of \$23,501,462 being used as state matching funds. Additional match bonds will be negotiated as needed to cover future capitalization grants. As of June 30, 2004, matching contributions are as follows:

	<u>Cumulative State Match as of June 30, 2003</u>	<u>2004 Contribution</u>	<u>Cumulative State Match as of June 30, 2004</u>
State cash contribution	\$26,753,586		\$26,753,586
Revenue bond proceeds	23,500,407	\$1,055	23,501,462
Total	<u>\$50,253,993</u>	<u>\$1,055</u>	<u>\$50,255,048</u>

MUNICIPAL FACILITIES REVOLVING LOAN FUND

<u>Components of Net Assets</u>	<u>Amount</u>
Capital contributions (cash only):	
Environmental Protection Agency	\$224,428,475
State of Louisiana match	26,753,586
Total cash contributions	<u>251,182,061</u>
Cumulative loan interest earnings	44,706,926
Cumulative treasury interest earnings	14,231,423
Administrative fee deposit	260,911
Cumulative administrative expenses	(9,242,856)
Cumulative bond costs	<u>(499,591)</u>
Total	<u>49,456,813</u>
Total net assets - unrestricted	<u><u>\$300,638,874</u></u>

8. OPERATING EXPENSES

Administrative Expenses

Four percent of the federal grant amounts awarded by the EPA are allocated to fund the administrative cost of operating the revolving loan fund. The following schedule presents each grant, the 4% amount allocated from each grant, the cumulative expenses incurred and drawn in administering the program, and the amount available to be drawn from the EPA for future administrative expenses.

<u>Federal Grant Year</u>	<u>Available 4% Set-Aside</u>	<u>State Fiscal Year</u>	<u>Expenses Incurred</u>	<u>Available for Administration</u>
1988	\$480,000			\$480,000
1989	414,751	1989	\$1,597	893,154
1990	429,011	1990	11,634	1,310,531
1991	902,429	1991	37,322	2,175,638
1992	854,374	1992	467,803	2,562,209
1993	845,167	1993	531,698	2,875,678
1994	524,415	1994	549,953	2,850,140
1995	541,609	1995	592,145	2,799,604
1996	887,171	1996	605,514	3,081,261
1997	272,816	1997	612,299	2,741,778
1998	887,606	1998	724,915	2,904,469
1999	592,163	1999	817,220	2,679,412
2000	590,155	2000	777,592	2,491,975
2001	589,450	2001	778,657	2,302,768
2002		2002	891,306	1,411,462
2003	586,208	2003	946,488	1,051,182
2004		2004	896,713	154,469
			<u>896,713</u>	<u>154,469</u>
Total	<u>\$9,397,325</u>		<u>\$9,242,856</u>	

Bond Issuance Costs

Bond issuance costs were absorbed by bond proceeds and are therefore not required to be charged against the 4% administrative costs ceiling, in accordance with 40 CFR 35.3120(g)(2).

9. ADMINISTRATIVE FEES

Annually, the MFRLF assesses a .5% administrative fee on all outstanding loan balances. Federal law allows the state to charge additional fees to supplement the 4% allowed from the fund itself to cover future excess administrative costs. These funds are deposited in the state treasury and accounted for outside the State Revolving Fund and are therefore 100% available for use. As of June 30, 2004, administrative fees are as follows:

Cash in state treasury, June 30, 2003	\$6,521,126
Current year revenue:	
.5% administrative fees	995,120
Treasury interest on administrative fees	87,281
Decrease in fees due from municipalities	108,766
(Increase) in interest due from state treasury	<u>(2,328)</u>
Cash in state treasury, June 30, 2004	<u><u>\$7,709,965</u></u>

10. LITIGATION AND CLAIMS

Losses arising from judgments, claims, and similar contingencies are paid through the state's self-insurance fund operated by the Office of Risk Management, the agency responsible for the state's risk management program, or by legislative appropriation. The MFRLF has no lawsuits outstanding at June 30, 2004.

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**OTHER REPORTS REQUIRED BY
GOVERNMENT AUDITING STANDARDS AND THE
ENVIRONMENTAL PROTECTION AGENCY AUDIT GUIDE
FOR CLEAN WATER AND DRINKING WATER
STATE REVOLVING FUND PROGRAMS**

The following pages contain reports on internal control over financial reporting and on compliance and other matters as required by *Government Auditing Standards*, issued by the Comptroller General of the United States, and on internal control and compliance with requirements applicable to the Capitalization Grants for Clean Water State Revolving Funds in accordance with the *Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*.

MUNICIPAL FACILITIES REVOLVING LOAN FUND _____



STEVE J. THERIOT, CPA
LEGISLATIVE AUDITOR

OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

1600 NORTH THIRD STREET
POST OFFICE BOX 94397
TELEPHONE: (225) 339-3800
FACSIMILE: (225) 339-3870

June 16, 2005

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*

**MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA
Baton Rouge, Louisiana**

We have audited the financial statements of the Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund as of and for the year ended June 30, 2004, and have issued our report thereon dated June 16, 2005. 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 Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund's internal control over financial reporting 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 audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Compliance and Other Matters

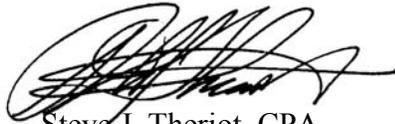
As part of obtaining reasonable assurance about whether the Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws and regulations, noncompliance with which could have a direct and material effect on the

MUNICIPAL FACILITIES REVOLVING LOAN FUND

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 Department of Environmental Quality and the federal awarding agency and is not intended to be and should not be used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this report is distributed by the Legislative Auditor as a public document.

Respectfully submitted,



Steve J. Theriot, CPA
Legislative Auditor

AOE:BQD:THC:dl

DEQMFRLF04



STEVE J. THERIOT, CPA
LEGISLATIVE AUDITOR

OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

1600 NORTH THIRD STREET
POST OFFICE BOX 94397
TELEPHONE: (225) 339-3800
FACSIMILE: (225) 339-3870

June 16, 2005

Report on Compliance With Requirements Applicable to the
Capitalization Grants for Clean Water State Revolving Funds
and on Internal Control Over Compliance in Accordance
With the *Environmental Protection Agency Audit Guide for
Clean Water and Drinking Water State Revolving Fund Programs*

**MUNICIPAL FACILITIES REVOLVING LOAN FUND
DEPARTMENT OF ENVIRONMENTAL QUALITY
STATE OF LOUISIANA**
Baton Rouge, Louisiana

Compliance

We have audited the compliance of the Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund with the types of compliance requirements that are applicable to the Capitalization Grants for Clean Water State Revolving Funds (CFDA 66.458) for the year ended June 30, 2004, as specified by the *Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*. Compliance with the requirements of laws, regulations, contracts, and grants applicable to this federal program is the responsibility of management of the Louisiana Department of Environmental Quality. Our responsibility is to express an opinion on the Municipal Facilities Revolving Loan Fund's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the *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 Municipal Facilities Revolving Loan 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 Municipal Facilities Revolving Loan Fund's compliance with those requirements.

MUNICIPAL FACILITIES REVOLVING LOAN FUND

In our opinion, the Louisiana Department of Environmental Quality - Municipal Facilities Revolving Loan Fund complied, in all material respects, with the requirements referred to previously that are applicable to its Capitalization Grants for Clean Water State Revolving Funds for the year ended June 30, 2004. However, the results of our auditing procedures disclosed the following instance of noncompliance with those requirements.

Payroll Costs Improperly Charged

The Department of Environmental Quality (DEQ), Municipal Facilities Revolving Loan Fund, did not allocate all payroll costs charged to the Capitalization Grants for Clean Water State Revolving Funds (CFDA 66.458) in accordance with federal regulations.

The Office of Management and Budget Circular A-87 states that costs are allowable if they are reasonable and necessary for the proper and efficient performance and administration of the program, are allocated to a particular program to the extent of the relative benefits received, and are appropriately documented. The costs of fringe benefits, such as annual leave, sick leave, holidays, and other similar benefits, are allowable if the costs are equitably allocated to all related activities.

During fiscal year 2004, payroll expenditures totaling \$10,217 were charged to the federal program for leave taken by two employees that should have been allocated to state activities, and therefore, we questioned these costs. These errors occurred because of management oversight. Failure to ensure the proper allocation of payroll costs increases the risk that the federal program could be overcharged.

Management of DEQ should allocate payroll costs equitably to the federal program as required by federal regulations. Management should also consult with the U.S. Environmental Protection Agency regarding the resolution of the cited questioned costs. Management concurred with the finding and recommendation and outlined a plan of corrective action (see Appendix A).

Internal Control Over Compliance

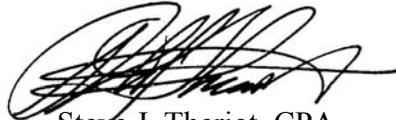
Management of the Department of Environmental Quality - Municipal Facilities Revolving Loan Fund is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to this federal program. In planning and performing our audit, we considered the Department of Environmental Quality - Municipal Facilities Revolving Loan Fund's internal control over compliance with requirements that could have a direct and material effect on its Capitalization Grants for Clean Water State Revolving Funds (CFDA 66.458), in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on the internal control over compliance in accordance with the *Environmental Protection Agency Audit Guide for Clean Water and Drinking Water State Revolving Fund Programs*.

REPORT ON COMPLIANCE AND INTERNAL CONTROL

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 this 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 controls over compliance and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of management of the Department of Environmental Quality and the federal awarding agency and is not intended to be and should not be used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this report is distributed by the Legislative Auditor as a public document.

Respectfully submitted,



Steve J. Theriot, CPA
Legislative Auditor

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Management's Corrective Action
Plan and Response to the
Finding and Recommendation

MUNICIPAL FACILITIES REVOLVING LOAN FUND _____



State of Louisiana
Department of Environmental Quality



KATHLEEN BABINEAUX BLANCO
GOVERNOR

MIKE D. McDANIEL, Ph.D.
SECRETARY

February 10, 2005

Mr. Steve J. Theriot, CPA
Office of Legislative Auditor
Post Office Box 94397
Baton Rouge, LA 70804-9397

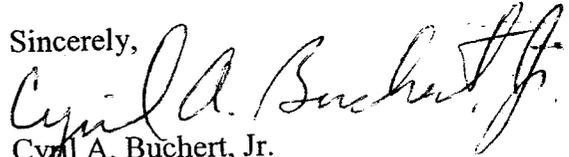
Dear Mr. Theriot:

This document represents a response by DEQ Management to the reportable audit finding "Payroll Cost Improperly Charged"

Management of the Municipal Facilities Revolving Loan Fund concurs with the finding. The department, when distributing other duties to employees previously working full time in this program, neglected to inform the employees involved of the correct coding of leave, holidays, and other similar benefits equitably to the other related activities.

Corrective action has already been implemented. Effective January 31, 2005, employees have been instructed to correctly code any leave, holiday, and other similar cost to non federal cost coding. Also, the incorrect coding for the previous pay periods during the current fiscal year (FY 2005) will be corrected via Pay Period Adjustment (PPA) documents. Darryl Serio, Accountant Administrator is the contact person responsible for ensuring that the corrective action necessary has been completed.

Sincerely,



Caryl A. Buchert, Jr.
Undersecretary

DS/



STEVE J. THERIOT, CPA
LEGISLATIVE AUDITOR

OFFICE OF
LEGISLATIVE AUDITOR
STATE OF LOUISIANA
BATON ROUGE, LOUISIANA 70804-9397

1600 NORTH THIRD STREET
POST OFFICE BOX 94397
TELEPHONE: (225) 339-3800
FACSIMILE: (225) 339-3870
www.lia.state.la.us

July 7, 2004

Dr. Mike McDaniel, Secretary
Department of Environmental Quality
Municipal Facilities Revolving Loan Fund
P.O. Box 4301
Baton Rouge, LA 70821-4301

Dear Dr. McDaniel:

We have enjoyed serving you in the audit of the Municipal Facilities Revolving Loan Fund's financial statements, as of and for the year ended June 30, 2003. Your audited financial statements are enclosed, and we have made all of the appropriate distributions. If you have any questions, please call our main office in Baton Rouge at 339-3800.

We appreciate the opportunity to serve you in this engagement. Your staff was most helpful to us, and we look forward to working with you on future engagements. If we can help you with any accounting, compliance, or auditing matters, please let us know.

Sincerely,

A handwritten signature in blue ink, appearing to read "Steve J. Theriot", is written over a horizontal line.

Steve J. Theriot, CPA
Legislative Auditor

A handwritten signature in black ink, appearing to read "Beth Davis", is written over a horizontal line.

Beth Davis, CPA
Audit Manager

SJT/ss

Enclosure

[MFRLF03]