



OFFICE OF INSPECTOR GENERAL

Catalyst for Improving the Environment

Audit Report

State of Oregon Clean Water State Revolving Fund Program Financial Statements for the Year Ended June 30, 2005

Report No. 2006-1-00021

January 12, 2006

Abbreviations

CWSRF	Clean Water State Revolving Fund
EPA	U.S. Environmental Protection Agency
GASB	Government Accounting Standards Board
ODEQ	Oregon Department of Environmental Quality
OIG	Office of Inspector General
SRF	State Revolving Fund



At a Glance

Catalyst for Improving the Environment

Why We Did This Audit

We performed this audit to determine:

- Whether the Oregon Clean Water State Revolving Fund Program's (the Program's) financial statements were fairly presented in all material respects;
- To what extent the Program's internal controls over financial reporting could be relied upon; and
- Whether the Program complied with applicable laws and regulations.

Background

The requirement for audited financial statements was enacted to help ensure that the Program had management practices, systems, and controls in place to provide reliable information for managing the Federally funded program.

For further information, contact our Office of Congressional and Public Liaison at (202) 566-2391.

To view the full report, click on the following link:

www.epa.gov/oig/reports/2006/20060112-2006-1-00021.pdf

State of Oregon Clean Water State Revolving Fund Program Financial Statements for the Year Ended June 30, 2005

What We Found

We rendered unqualified opinions on the Oregon Clean Water State Revolving Fund Program financial statements for the year ended June 30, 2005, and Oregon's compliance with applicable laws and regulations. We did not note any weaknesses in internal control that we consider to be material.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

OFFICE OF
INSPECTOR GENERAL

January 12, 2006

MEMORANDUM

SUBJECT: Auditor's Report for the State of Oregon
Clean Water State Revolving Fund Program
Financial Statements for the Year Ended June 30, 2005
Report No. 2006-1-00021

FROM: Michael A. Rickey /s/ *Michael A. Rickey*
Director for Assistance Agreement Audits

TO: Michael Bogert, Regional Administrator
EPA Region 10
Seattle, WA

Attached is a copy of the subject audit we sent to the State of Oregon. The audit contains reports on the financial statements, internal controls, and compliance requirements applicable to the State of Oregon Clean Water State Revolving Fund Program financial statements for the year ended June 30, 2005.

We issued an unqualified opinion on the financial statements and on the compliance requirements applicable to the State of Oregon Clean Water State Revolving Fund program. In addition, we did not note any matters involving the internal control system and operations that we consider to be material weaknesses.

Since we did not have any compliance matters or costs questioned, we are closing the audit report on issuance.

We have no objection to the release of this report to any member of the public upon request. The report contains no confidential business or proprietary information. If you have any questions or concerns, please contact Mr. William Dayton at (916) 498-6590 or Ms. Melinda Burks at (206) 553-6906.

Enclosure

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At a Glance

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UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

OFFICE OF
INSPECTOR GENERAL

**Independent Auditor's Report on the State of Oregon
Clean Water State Revolving Fund Program Financial Statements
for the Year Ended June 30, 2005**

We have audited the accompanying financial statements of the State of Oregon Clean Water State Revolving Fund Program (the Program) as of and for the year ended June 30, 2005. These financial statements are the responsibility of the Program's management. Our responsibility is to express opinions 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 financial statements referred to above are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of the Program. They do not purport to, and do not, present fairly the financial position of the State of Oregon as of June 30, 2005, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Program, as of June 30, 2005, and the changes in financial position and cash flows, where applicable, for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

Office of Inspector General
November 8, 2005

State of Oregon
Clean Water State Revolving Fund Program
Statement of Net Assets
June 30, 2005

<u>Assets</u>	<u>SRF</u>	<u>Administration</u>	<u>Total</u>
Current Assets:			
Cash and cash equivalents	\$ 81,882,351	\$ 5,227,382	\$ 87,109,733
Loan interest receivable	3,343,107		3,343,107
Loans receivable, current	<u>20,868,862</u>		<u>20,868,862</u>
Total current assets	<u>106,094,320</u>	<u>5,227,382</u>	<u>111,321,702</u>
Noncurrent Assets:			
Loans receivable, net of current	256,969,663		256,969,663
Deferred Expenses	<u>237,544</u>		<u>237,544</u>
Total noncurrent assets	<u>257,207,207</u>		<u>257,207,207</u>
Total Assets	<u>\$ 363,301,527</u>	<u>\$ 5,227,382</u>	<u>\$ 368,528,909</u>
<u>Liabilities and Net Assets</u>			
Current Liabilities:			
Accounts payable		\$ 3,715	\$ 3,715
Payroll payable		47,867	47,867
Construction costs payable	\$ 443,371		443,371
Due to other funds		9,243	9,243
Bond interest payable	228,930		228,930
Bonds payable	<u>850,000</u>		<u>850,000</u>
Total current liabilities	<u>1,522,301</u>	<u>60,825</u>	<u>1,583,126</u>
Noncurrent Liabilities:			
Bonds payable, net of current	<u>15,505,000</u>		<u>15,505,000</u>
Total noncurrent liabilities	<u>15,505,000</u>		<u>15,505,000</u>
Total liabilities	<u>17,027,301</u>	<u>60,825</u>	<u>17,088,126</u>
Net assets:			
Restricted	<u>346,274,226</u>	<u>5,166,557</u>	<u>351,440,783</u>
Total liabilities and net assets	<u>\$ 363,301,527</u>	<u>\$ 5,227,382</u>	<u>\$ 368,528,909</u>

State of Oregon
Clean Water State Revolving Fund Program
Statement of Revenues, Expenses, and Changes in Net Assets
For the Year Ended June 30, 2005

	<u>SRF</u>	<u>Administration</u>	<u>Total</u>
Operating Revenues:			
Loan interest	\$ 9,233,418		\$ 9,233,418
Investment earnings	1,917,031	\$ 109,544	2,026,575
Loan fees		<u>1,068,473</u>	<u>1,068,473</u>
Total operating revenues	<u>11,150,449</u>	<u>1,178,017</u>	<u>12,328,466</u>
Operating Expenses:			
Bond interest	1,356,265		1,356,265
Other bond costs	91,619		91,619
Salaries and benefits		701,025	701,025
Services and supplies		103,424	103,424
Indirect costs		<u>134,597</u>	<u>134,597</u>
Total operating expenses	<u>1,447,884</u>	<u>939,046</u>	<u>2,386,930</u>
Operating Income	9,702,565	238,971	9,941,536
Nonoperating Revenues (Expenses)			
EPA grants received	16,048,936		16,048,936
Transfers in (out)	<u>(485,483)</u>	<u>485,483</u>	<u>0</u>
Total nonoperating revenues (expenses)	<u>15,563,453</u>	<u>485,483</u>	<u>16,048,936</u>
 Change in net assets	 <u>25,266,018</u>	 <u>724,454</u>	 <u>25,990,472</u>
Net assets, beginning of year	341,540,655	4,442,103	345,982,758
Prior Period Adjustment			
Effect of assumption of general obligation bonds since June 30, 2003	<u>(20,532,447)</u>		<u>(20,532,447)</u>
Net assets, beginning of year, adjusted	<u>321,008,208</u>	<u>4,442,103</u>	<u>325,450,311</u>
Net assets, end of year	<u>\$ 346,274,226</u>	<u>\$ 5,166,557</u>	<u>\$351,440,783</u>

**State of Oregon
Clean Water State Revolving Fund Program
Statement of Cash Flows
For the Year Ended June 30, 2005**

Cash flows from operating activities:	
Cash received from loan interest repayments	\$ 9,066,091
Cash received from loan principal repayments	13,171,290
Cash disbursed to borrowers	(40,238,856)
Cash received from loan fees	1,068,473
Interest payments on match bonds	(1,127,335)
Cash received from Treasury interest credits	2,026,575
Cash payments to:	
Vendors	(108,895)
Employees	(711,066)
Indirect cost	(125,394)
Net cash used by operating activities	<u>(16,979,117)</u>
Cash flows from noncapital financing activities:	
Net cash provided by noncapital financing activities	_____
Cash flows from capital and related financing activities:	
Funds received from EPA	16,128,447
Proceeds from sale of bonds	5,988,389
Principal payments on match bonds	<u>(10,495,000)</u>
Net cash provided by capital and related financing activities	<u>11,621,836</u>
Cash flows from investing activities:	
Net cash provided by investing activities	_____
Net decrease in cash	(5,357,281)
Cash and cash equivalents, beginning of year	<u>92,467,014</u>
Cash and cash equivalents, end of year	<u>\$ 87,109,733</u>

State of Oregon
Clean Water State Revolving Fund Program
Statement of Cash Flows
For the Year Ended June 30, 2005

Reconciliation of operating income to net cash used by operating activities:

Operating income	\$ 9,941,536
Amortization of bond costs	91,619
Adjustments to reconcile operating income to net cash used by operating activities:	
(Increase) in loan interest receivable	(167,327)
(Increase) in loans receivable	(27,457,748)
Increase in construction costs payable	390,182
(Decrease) in accounts payable	(5,477)
(Decrease) in payroll payable	(11,075)
Increase in amount due to other funds	10,243
Increase in bond interest payable	<u>228,930</u>
Net cash used by operating activities	<u><u>\$ (16,979,117)</u></u>

State of Oregon
Clean Water State Revolving Fund Program
Notes to the Financial Statements

1. Organization of the Fund

The Oregon Clean Water State Revolving Fund (the Fund) was established pursuant to Oregon Revised Statutes 468.423 – 468.440. The purpose of the Fund is to provide low interest loans to local governments for constructing wastewater treatment facilities, implementing nonpoint source pollution management plans, and the design and implementation of estuary management plans. The loan repayment period is a maximum of 20 years, and all repayments, including interest and principal, must be credited to the State Revolving Fund.

The Fund is administered by the State of Oregon's Department of Environmental Quality (ODEQ). The SRF program consists of several funds to record loan and related activity and an administrative fund that collects loan fees and pays the operating costs of the program, and are collectively referred to as the Fund. ODEQ's primary responsibilities for the Fund include obtaining capitalization grants from EPA, soliciting potential interested parties for loans, negotiating loan agreements with local communities, reviewing and approving payment requests from loan recipients, monitoring the loan repayments, and conducting inspection and engineering reviews to ensure compliance with all applicable laws, regulations, and program requirements.

The ODEQ charges the Fund for staff time spent on SRF activities, and the Fund pays those expenses from the Administration fund. The charges include the salaries and benefits of the employees, as well as indirect costs allocated to the Fund. The rate of indirect cost is negotiated annually with the EPA. Employees charging time to the Fund are covered by the benefits available to Oregon State Employees. The Fund is also charged indirect costs through the cost allocation plan for general state expenses.

The Fund financial statements, footnotes, and required supplemental information are presented for the U.S. Environmental Protection Agency. The Fund is included in the Oregon general purpose financial statements as a special revenue fund which uses the modified accrual basis of accounting. Due to differences in reporting methods, there may be differences between the amounts reported in these financial statements and the general purpose financial statements.

2. Summary of Significant Accounting Policies

Basis of Accounting

The financial statements for the Fund are presented as an enterprise fund. As such, the Fund is accounted for using the flow of economic resources measurement focus and is maintained on the accrual method of accounting. Under the accrual method of accounting, revenues are recognized when earned and expenses are recorded at the time the liabilities are incurred. All assets and liabilities associated with the operations of the Fund are included on the balance sheet. The State has elected to follow the accounting pronouncements of the Governmental Accounting Standards Board (GASB), as well as statements issued by the Financial Accounting Standards Board on or before November 30, 1989, unless the pronouncements conflict with or contradict GASB pronouncements.

Cash and Cash Equivalents

All monies of the Fund are deposited with the Oregon Treasurer's Office which is responsible for maintaining these deposits in accordance with Oregon law. The Fund considers all such deposits to be cash. Investment interest earnings on these deposits are received by the Fund on a monthly basis. According to State law, the Treasurer is responsible for maintaining the cash balances and investing excess cash of the Fund, as further discussed in Note 3. Consequently, management of the Fund does not have any control over the investment of the excess cash. The statement of cash flows considers all funds deposited with the Treasurer to be cash or cash equivalents, regardless of actual maturities of the underlying investments.

**State of Oregon
Clean Water State Revolving Fund Program
Notes to the Financial Statements**

2. Summary of Significant Accounting Policies (continued)

Loans Receivable

The loans are funded by Federal capitalization grants, State matching funds, general obligation and revenue bonds, loan repayments, and fund earnings. The SRF monies are disbursed to borrowers on a cost reimbursement basis. When borrowers have incurred qualifying expenses, they request a loan disbursement from the Fund, and at that time, a disbursement is made and recorded in the Fund accounting records. Interest begins accruing when funds are disbursed to the borrower. After the final disbursement, repayment begins with an interest only payment. Full repayment must be received by the Fund within 20 years. There is no provision for uncollectible accounts, as all repayments are current, and program management believes all loans will be repaid according to the loan terms. There have been no loan defaults in the program since its inception.

3. Cash and Cash Equivalents

All cash in the Fund is deposited with the State Treasurer who is responsible for maintaining and investing the pooled cash balances in accordance with State laws. The Treasurer is required to maintain a mix of investments in order to allow funds to be withdrawn at any time to meet normal operating needs. The Fund's share of the investment income is based on the average daily balance for the period and is credited to the Fund monthly. Details of the investments can be obtained from the State Treasurer's Office.

All cash and investments are stated at cost, which approximates fair market value. Investments held by the State Treasurer's Office are not categorized because they are not evidenced by securities that exist in physical or book entry form.

	Carrying Amount	Market Value
Not subject to categorization:		
Deposited with State Treasurer's Office	\$ 87,109,733	\$ 87,109,733

4. Loans Receivable

The Fund makes loans to qualified entities at interest rates ranging from zero percent to the market rate. Interest rates vary depending on the length of the loan, the type of loan, and program rules. Prior to 1995 rates were either zero percent or three percent, depending on the length of the repayment period. Between 1995 and 2003 the interest rate for facilities planning was one-half the bond rate, and the interest rate for design and construction was the greater of two-thirds the bond rate or the bond rate minus two percent. In May of 2003, interest rates were modified to be based on loan terms. Rates range from 25% of the bond rate for 5 year loans to 65% of the bond rate for 20 year loans. Recipients make semiannual or, in some cases, annual payments, generally starting six months after project completion. Details of loans receivable as of June 30, 2005 are as follows:

	Loan Authorized	Remaining Commitment	Outstanding Balance
Completed projects	\$ 359,077,807	\$ 0	\$ 237,127,067
Projects in progress	168,941,268	129,491,762	40,711,458
Totals	\$ 528,019,075	\$129,491,762	277,838,525
Less amounts due within one year			20,868,862
Loans receivable, June 30, 2005			\$ 256,969,663

Loans mature at various intervals through June 1, 2026. The scheduled minimum principal repayments in future years are as follows:

State of Oregon
Clean Water State Revolving Fund Program
Notes to the Financial Statements

4. Loans Receivable (continued)

Year ending June 30:	<u>Amount</u>
2006	\$ 20,868,862
2007	16,397,183
2008	16,306,544
2009	16,839,853
2010	17,175,556
Thereafter	<u>190,250,527</u>
Total	<u>\$277,838,525</u>

Loans to Major Local Agencies:

As of June 30, 2005, the Fund has made loans to 14 local governments that totaled \$10,000,000 or more, and in the aggregate, exceeded \$340,000,000. The outstanding balances of these loans represent approximately 65 percent of the total loans receivable, as follows:

<u>Borrower</u>	<u>Authorized Loan Amount</u>	<u>Outstanding</u>	<u>Status</u>
City of Albany	\$ 49,286,394	1,127,562	New/Repay.
City of Ashland	23,920,068	\$21,659,513	Repayment
City of Brookings	13,100,000	12,032,716	Repayment
City of Corvallis	21,963,693	18,406,188	Repayment
City of Dallas	14,880,000	12,078,316	Repayment
City of Eugene	25,592,592	2,069,417	Repayment
City of Florence	12,279,155	10,424,646	Repayment
City of Gresham	42,359,498	23,716,463	Repayment
City of Newport	20,228,883	18,626,921	Repayment
City of Ontario	13,971,689	8,278,581	Repayment
City of Portland	33,791,673	6,162,969	Paid/Active
City of Prineville	18,267,286	12,639,663	New/Repay.
City of Redmond	21,138,406	5,383,352	Repay/Active
City of Woodburn	<u>30,349,671</u>	<u>25,689,276</u>	Repayment
TOTAL	<u>\$ 341,129,008</u>	<u>\$ 178,295,584</u>	

5. Fixed Assets

The only fixed assets are equipment. During fiscal year 2005 there were no purchases of equipment, and the existing CWSRF loan program capital assets have all been fully depreciated.

6. Bonds Payable

In July 2003, EPA allowed the SRF to use Fund assets to pay the principal and interest on \$23,765,000 of general obligation bonds that were previously issued by the State to provide the 20 percent state matching funds as required by the Clean Water Act. The details of such bonds at June 30, 2005 are as follows:

State Match Bonds:

	<u>Balance</u>	<u>Current</u>	<u>Long-term</u>
Series 1995B, General Obligation Pollution Control Bonds, interest of 4.7% to 5.25% due semi-annually, principal due annually to November 1, 2015.	\$ 3,325,000	\$ 230,000	\$ 3,095,000

State of Oregon
Clean Water State Revolving Fund Program
Notes to the Financial Statements

6. Bonds Payable (continued)

Series 1997A, General Obligation Pollution Control Bonds, interest of 3.8% to 5.0% due semi- annually, principal due annually to November 1, 2017.	6,035,000	335,000	5,700,000
Series 2000A, General Obligation Pollution Control Bonds, interest of 4.15% to 5.50% due semi- annually, principal due annually to August 1, 2020.	<u>6,995,000</u>	<u>285,000</u>	<u>6,710,000</u>
Totals	<u>\$ 16,355,000</u>	<u>\$ 850,000</u>	<u>\$ 15,505,000</u>

7. Federal Grants and State Match

The Fund is capitalized by Capitalization Grants for SRF from the EPA. These grants have been awarded annually, beginning in federal fiscal year 1989. The State of Oregon must also contribute an amount equal to 20 percent of the federal capitalization amount, as discussed below. As of June 30, 2005, EPA has awarded capitalization grants in the amount of \$263,489,612 to the State of Oregon, of which \$251,316,671 has been drawn for loans and administrative expenses. The following summarizes the capitalization grant awards, amounts drawn on each grant as of the balance sheet date, and balances available for loans and administrative costs:

	Grant Amount	Total Draws As of June 30, 2004	2005 Draws	Total Draws as of June 30, 2005	Grant Funds Available June 30, 2005
1989-2002	\$ 221,383,526	\$ 221,383,526	\$ 0	\$ 221,383,526	\$ 0
2003	14,962,068	13,804,698	1,157,370	14,962,068	0
2004	14,971,077	0	14,971,077	14,971,077	0
2005	12,172,941	0	0	0	12,172,941
Totals	<u>\$ 263,489,612</u>	<u>\$ 235,188,224</u>	<u>\$ 16,128,447</u>	<u>\$ 251,316,671</u>	<u>\$ 12,172,941</u>

Prior to 1993, Oregon's matching contribution was provided through appropriation of State general fund resources. Beginning in 1993, state matching funds were provided by issuing General Obligation Pollution Control Bonds. Between 1993 and 2003, Oregon issued \$29,980,000 in state match bonds and transferred the proceeds plus interest to the SRF as state match. In July 2003, EPA allowed the SRF to assume \$23,765,000 of previously issued bonds, and principal and interest payments on those bonds to be paid from interest earnings of the SRF. Activity on bonds assumed by the SRF since July 2003 is as follows:

Bond Issue	Balance Transferred July 1, 2003	Principal Paid 2004	Principal Paid 2005	Balance June 30, 2005
1993A	1,865,000	1,865,000		0
1994A	3,965,000	280,000	3,685,000	0
1995B	3,755,000	210,000	220,000	3,325,000
1997A	6,660,000	305,000	320,000	6,035,000
2000A	7,520,000	255,000	270,000	6,995,000
	<u>\$ 23,765,000</u>	<u>\$ 2,915,000</u>	<u>\$ 4,495,000</u>	<u>\$ 16,355,000</u>

**State of Oregon
Clean Water State Revolving Fund Program
Notes to the Financial Statements**

7. Federal Grants and State Match (continued)

Interest paid on bonds transferred to the SRF was approximately \$745,000 in 2004 and \$897,000 in 2005.

Since July 2003, Oregon has issued bonds to provide state match, with all principal and interest on such bonds being paid by the SRF. The details of such bonds are as follows:

Bond Issue	Issued	Principal Paid 2004	Principal Paid 2005	Balance June 30, 2005
2003C	\$ 3,000,000	\$ 3,000,000		\$ -
2004A	6,000,000		\$ 6,000,000	-
	<u>\$ 9,000,000</u>	<u>\$ 3,000,000</u>	<u>\$ 6,000,000</u>	<u>\$ -</u>

The effect on the state matching funds previously contributed by the State is as follows:

	<u>June 30, 2005</u>
Oregon State Matching Contribution	\$ 47,277,572
Reduce state match for transfers from bond fund	<u>(26,429,045)</u>
State Match, Adjusted	<u>\$ 20,848,527</u>

8. Loan Fees

In order to support administration and project management costs, loan fees are assessed on all loans originating after 1992. A loan origination fee of 1.5 percent is assessed at the beginning of the repayment period, and an annual fee of 0.5 percent is assessed on the outstanding balance. The fees are deposited to an account outside the Fund and will be used only for administrative and project management costs.

In May 2003, the Environmental Quality Commission (EQC) approved changes to the program's administrative rules. One of the approved changes is the elimination of the 1.5% loan processing fee that has been charged on all loans. This fee is no longer charged. Also, fees on planning loans will not be assessed, in order to encourage Oregon communities to complete more planning.

9. Contingencies, Related Parties, and Subsequent Events

Contingencies

The Fund is exposed to various risks of loss related to torts, thefts of assets, errors or omissions, injuries to state employees while performing Fund business, or acts of God. The State maintains insurance for all risks of loss which is included in the indirect costs allocated to the Fund.

In previous years the State of Oregon has been named in suits against CWSRF borrowers, by citizens either claiming unlawful sewer rate increases or unlawful debt. These suits have been decided in favor of our borrowers and the State of Oregon, and we are unaware of any such contingencies in existence at this time.

**State of Oregon
Clean Water State Revolving Fund Program
Notes to the Financial Statements**

9. Contingencies, Related Parties, and Subsequent Events (continued)

Related Parties

There are no related party transactions with or related amounts receivable from management of the Fund.

Subsequent Events

No events occurred subsequent to the balance sheet date that came to our attention which require adjustment to, or disclosure in, the financial statements.



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

OFFICE OF
INSPECTOR GENERAL

**Independent Auditor's 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***

We have audited the financial statements of the State of Oregon Clean Water State Revolving Fund Program (the Program) as of and for the year ended June 30, 2005, and have issued our report thereon dated November 8, 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 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 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 Program'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 the determination of financial statement amounts. This included tests of specific program requirements governing allowability for specific activities, allowable types of assistance, State matching, period of availability of funds and binding commitments, cash management, program income, and subrecipient monitoring that are applicable to the Program for the year ended June 30, 2005.

The management of the Program is responsible for the Program's compliance with those requirements. Our responsibility is to express an opinion on those requirements based on our audit. An audit includes examining, on a test basis, evidence about the Program's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the Program complied, in all material respects, with the specific program requirements that are applicable to the Program for the year ended June 30, 2005.

This report is intended solely for the information and use of management of the Program and the U.S. Environmental Protection Agency, and is not intended to be and should not be used by anyone other than these specified parties.

Office of Inspector General
November 8, 2005

Distribution

EPA Region 10

Regional Administrator
Director, Water Division
State Revolving Fund Coordinator
Audit Followup Coordinator

EPA Headquarters

Director, Grants Administration Division
Director, Financial Management Division
Director, Office of Grants and Debarment
Agency Followup Coordinator
State Revolving Fund Audit Manager
State Revolving Fund Branch, Office of Water

State of Oregon

Division of Water Quality, Oregon Department of Environmental Quality