



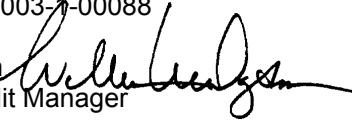
ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C

OFFICE OF
INSPECTOR GENERAL

March 27, 2003

Memorandum

Subject: Auditor's Report for the New Hampshire Drinking Water State Revolving Fund Program (the Program) as of June 30, 2002
Audit Report No.2003-1-00088

From: William M. Dayton 
National SRF Audit Manager

To: Robert W. Varney
Regional Administrator
EPA, Region 1
Boston, MA

Attached is a copy of the subject audit we sent to the State of New Hampshire. The audit contains reports on the financial statements, internal controls, and compliance requirements applicable to the Drinking Water State Revolving Fund (SRF) program in New Hampshire for the year ended June 30, 2002.

We issued an unqualified opinion on the financial statements and on the compliance requirements applicable to the Drinking Water SRF program. We qualified our opinion on the compliance requirements applicable to the SRF program because the New Hampshire Drinking Water State Revolving Fund did not comply with certain compliance matters required by the Safe Drinking Water Act and regulations. We did not note any matters involving the internal control system and operations that we consider to be reportable conditions. In response to the draft audit report, management agreed with all of our compliance and internal control issues, and are taking appropriate steps to correct the deficiencies.

In accordance with EPA directive 2750, the Action Official is required to take action on the findings and recommendations in this report within 150 days.

The OIG has 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 regarding this matter, please feel free to contact me at (916) 498-6590 or Mr. Paul Felz at (303) 312-6270.

Attachment



ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C

OFFICE OF
INSPECTOR GENERAL

March 27, 2003

Mr. Robert Monaco, Acting Commissioner
New Hampshire Department of Environmental Services
6 Hazen Drive
Concord, NH 03301

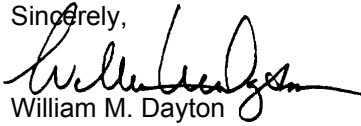
Re: Audit Reports of the Financial Statements of the New Hampshire Drinking Water State Revolving Fund Program for the year ended June 30, 2002

Dear Mr. Monaco:

Enclosed please find an electronic copy of the audited financial statements for the New Hampshire Drinking Water State Revolving Fund Program for the year ended June 30, 2002. We made certain adjustments and reclassifications, to which you have agreed, in order to have the financial statements follow EPA's current reporting guidelines, which are accordance with generally accepted accounting principles

We would like to thank you and your staff for the cooperation and courtesies we received during our audit. Please feel free to call me at (916) 498-6590 or Mr. Paul Felz at (303) 312-6270 should you have any comments or questions.

Sincerely,


William M. Dayton
National SRF Audit Manager



OIG

OFFICE OF INSPECTOR GENERAL

Catalyst for Improving the Environment

Audit Report

New Hampshire Drinking Water State Revolving Fund Program

**Financial Statements with
Independent Auditor's Report, June 30, 2002**

Audit Report Number 2003-1-00088

Issued March 27, 2003



Kancamagus Highway, New Hampshire

**New Hampshire Drinking Water State Revolving Fund
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ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C

OFFICE OF
INSPECTOR GENERAL

Independent Auditor's Report

To: Mr. Robert Monaco, Acting Commissioner
New Hampshire Department of Environmental Services

We have examined the accompanying balance sheet of the New Hampshire Drinking Water State Revolving Fund Program (the Program) as of June 30, 2002, the related statement of revenues, expenses, and changes in net assets, and the statement of cash flows for the year then ended. These financial statements are the responsibility of the Program's management. Our responsibility is to express an opinion on these financial statements based on our audit.

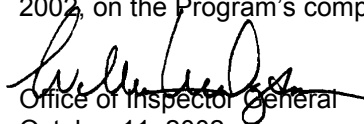
We conducted our audit in accordance with generally accepted auditing standards in the United States of America and *Government Auditing Standards* issued by the Comptroller General of the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance 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.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Program as of June 30, 2002, and the results of its activities and its cash flows for the year then ended in conformity with generally accepted accounting principles in the United States of America.

Our audit was conducted for the purpose of forming an opinion on the combined financial statements taken as a whole. The supplemental information is presented for purposes of additional analysis of the combined financial statements. The supplemental information has been subjected to the auditing procedures applied in the audit of the combined financial statements and, in our opinion, is fairly stated in all material respects in relation to the combined financial statements taken as a whole.

As discussed in Note 1, the financial statements referred to above are intended to present the financial position and results of operations of the Program, a component of the general fund of the State of New Hampshire. These statements are not intended to present the financial position or results of operations for the State of New Hampshire or the New Hampshire Department of Environmental Services, of which the Program is a part. Certain supplementary information referred to as Management Discussion and Analysis, although not a required part of the basic financial statements, has been omitted for this program-specific financial presentation.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 11, 2002, on our consideration of the Program's internal control structure and a report dated October 11, 2002, on the Program's compliance with laws and regulations.


Office of Inspector General
October 11, 2002

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund

Balance Sheet
As of June 30, 2002

Assets	SRF	Management	Total (Memorandum) (Only)
Current Assets:			
Cash and cash equivalents	\$ 2,825,805	\$ 128,048	\$ 2,953,853
Current receivables:			
Interest	219,719		219,719
Current portion of loans receivable:	721,990		721,990
Due from Federal government	101,571		101,571
Due from other funds	115,779		115,779
Total current receivables	1,159,059	-	1,159,059
Total current assets	3,984,864	128,048	4,112,912
Non-Current Assets:			
Loans receivable, net of current portion:	19,759,860		19,759,860
Allowance for Principal Forgiveness	(1,644,298)		(1,644,298)
Total non-current assets	18,115,562	-	18,115,562
Total Assets	22,100,426	128,048	22,228,474
Liabilities and Net Assets			
Liabilities:			
Accounts payable	210,145		210,145
Construction costs payable	17,402		17,402
Accrued payroll	7,205		7,205
Unearned Interest Income	134		134
Total liabilities	234,886	-	234,886
Net assets:			
Unrestricted	21,865,540	128,048	21,993,588
Total liabilities and net assets	\$ 22,100,426	\$ 128,048	\$ 22,228,474

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

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Statement of Revenues, Expenses and Changes in Net Assets
For the Year Ended June 30, 2002

	<u>SRF</u>	<u>Management</u>	<u>Total (Memorandum) (Only)</u>
Operating Revenues:			
Loan interest	\$ 413,481		\$ 413,481
Loan fees		104,212	104,212
Grant revenues	1,768,070		1,768,070
Investment earnings	50,426		50,426
Total operating revenues	<u>2,231,977</u>	<u>104,212</u>	<u>2,336,189</u>
Operating Expenses:			
Program administration	338,656	-	338,656
Technical assistance	174,763	-	174,763
State program management	411,991	-	411,991
Source water protection/capacity development	842,660	-	842,660
Principal forgiveness	1,633,888	-	1,633,888
Total operating expenses	<u>3,401,958</u>	<u>-</u>	<u>3,401,958</u>
Operating income (loss)	(1,169,981)	104,212	(1,065,769)
Capital Contributions:			
Federal contribution	7,347,441		7,347,441
State of New Hampshire contribution	1,878,348		1,878,348
Total capital contributions	<u>9,225,789</u>		<u>9,225,789</u>
Change in net assets	8,055,808	104,212	8,160,020
Net assets, beginning of year	<u>13,809,732</u>	<u>23,836</u>	<u>13,833,568</u>
Net assets, end of year	<u>\$ 21,865,540</u>	<u>\$ 128,048</u>	<u>\$ 21,993,588</u>

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

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund

Statement of Cash Flows
For the Year Ended June 30, 2002

Cash flows from operating activities:	
Interest receipts	\$ 302,656
Loan fee receipts	104,212
Receipts from operating grants	1,843,874
Receipts from investments	57,617
Loan principal repayments	568,752
Payments for program administration	(322,258)
Payments for technical assistance	(171,549)
Payments for state program management	(464,768)
Payments for source water protection/capacity development	(885,299)
Disbursements on loans	<u>(9,225,789)</u>
Net cash (used) by operating activities	<u>(8,192,553)</u>
Cash flows from capital and related financing activities:	
Capitalization grants received from EPA	7,347,441
Funds received from the State of New Hampshire	<u>1,878,348</u>
Net cash provided by capital and related financing activities	<u>9,225,789</u>
Increase (decrease) in cash and cash equivalents	1,033,236
Cash and cash equivalents, beginning of year	<u>1,920,618</u>
Cash and cash equivalents, end of year	<u><u>\$ 2,953,853</u></u>
Reconciliation of operating (loss) to net cash used by operating	
Operating (loss)	\$ (1,065,769)
Capitalized Interest	(7,366)
Loan principal forgiveness	1,633,888
Change in assets and liabilities:	
Interest Receivable	(96,289)
Due from Federal government	187,150
Due from other funds	(115,756)
Accounts payable	(54,363)
Accrued payroll	(17,032)
Unearned interest income	21
Loan repayments	568,752
Loan disbursements	<u>(9,225,789)</u>
Net cash (used) by operating activities	<u><u>\$ (8,192,553)</u></u>

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

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Notes to Financial Statements

1. Organization of the Program

The New Hampshire Drinking Water State Revolving Fund Program (the Program) was established pursuant to section 1452 (a) of the Safe Drinking Water Act amendments of 1996 and RSA-486:14. The purpose of the SRF is to provide low interest loans to assist public water systems for financing the costs of infrastructure needed to ensure safe drinking water. The loan repayment period ranges from five to twenty years, and all repayments, including interest and principal, must be credited to the Program.

The SRF program is administered by the State of New Hampshire's Department of Environmental Services (NHDES), and consists of a loan fund to record loan and related activity and an administrative fund that collects fees and will in the future, pay the operating costs of the program, and are collectively referred to as the Program. The Department's primary responsibilities for the SRF include obtaining capitalization grants from the Environmental Protection Agency (EPA), soliciting potential interested parties for loans, negotiating loan agreements with local water systems, 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. In addition to the loan fund, states are allowed to take portions of the capitalization grants for non-infrastructure project activities, or "set-asides", which further the intent of the Safe Drinking Water Act. Program activities (set-asides) include program administration and management, source water protection, operator certification, capacity development and water system technical assistance.

The Program has no full time employees. On a monthly basis the NHDES charges the Program for time spent on SRF activities by its employees. The charges include the salaries and benefits of the employees, as well as indirect costs allocated to the Program. Employees charging time to the Program are covered by the benefits available to State of New Hampshire Employees. The fund is also charged indirect costs through a cost allocation plan agreement between NHDES and U.S. EPA, which is renewed annually.

The Program's financial statements, footnotes, and related schedules are presented for the U.S. Environmental Protection Agency. The Program is included in the State of New Hampshire's basic financial statements as a part of the State's general 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 State's basic financial statements.

2. Summary of Significant Accounting Policies

Basis of Accounting

The financial statements for the Program are presented as an enterprise fund. As such, the Program 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 Program 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.

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Notes to Financial Statements

2. Summary of Significant Accounting Policies (continued)

Cash and Cash Equivalents

All monies of the Program are deposited with the New Hampshire State Treasurer's Office, which is responsible for maintaining these deposits in accordance with New Hampshire State law. The Program considers all such deposits to be cash. The Program on a monthly basis receives investment interest earnings on these deposits. According to State law, the Treasurer is responsible for maintaining the cash balances and investing excess cash of the Program, as further discussed in Note 3. Consequently, management of the Program 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.

Loans Receivable

The loans are funded by Federal capitalization grants and State matching funds. The SRF monies are disbursed to borrowers on a cost reimbursement basis. When the borrowers have incurred qualifying expenses, they request a loan disbursement from the Program, and at that time a disbursement is made. Interest begins accruing when funds are disbursed to the borrower. Repayment of the loan begins within six months to one year of construction completion. The Program must receive full repayment within twenty years of project completion. There is no allowance for uncollectible accounts, as all repayments are current, and management believes all loans will be repaid according to the loan terms.

New Hampshire provides subsidies for disadvantaged communities under the Disadvantaged System Program as outlined in Section 9 of the 2001 State of New Hampshire Drinking Water SRF Intended Use Plan. Subsidies are available in the form of principal forgiveness. This program only applies to infrastructure projects. The amount of principal forgiveness is determined when the aggregate principal loan amount is established and project is complete.

Contributed Capital

In accordance with generally accepted accounting principles (GAAP), funds received from EPA and the State of New Hampshire to capitalize the loan program are recorded as contributed capital. Funds received from EPA for reimbursement of set-aside expenses are treated as operating grants.

3. Cash and Cash Equivalents

All cash in the Program 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 Program's share of the investment income from the local government investment pool is based on the average daily balance for the period and is credited to the Program monthly. The short term investments of SRF funds are made with certificates of deposit and discounted notes which mature within six to nine months. Details of the investments can be obtained from the State Treasurer's Office.

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Notes to Financial Statements

3. Cash and Cash Equivalents (continued)

All cash and investment in the local government investment pool are stated at cost, which approximates fair market value. Investments in local government pools are not categorized because they are not evidenced by securities that exist in physical or book entry form.

	<u>Carrying Amount</u>
Not subject to categorization:	
Local government investment pool	\$1,325,805
Subject to categorization:	
Certificates of Deposit and Notes	<u>\$1,500,000</u>
Total	<u>\$2,825,805</u>

4. Loans Receivable

The Program makes loans to qualified entities at interest rates ranging from .1875 percent to 3.5840 percent. Interest rates are initially set in the original loan agreement, and then when the project is completed a supplemental loan agreement is made which fixes the final interest rate to be charged at the lower of the original loan agreement or prevailing market rate, per the following formula:

<u>Loan Term</u>	<u>Interest Rate</u>
5 years	25% of market minus 1%
10 years	50% of market minus 1%
15 years	75% of market minus 1%
20 years	80% of market minus 1%

As of June 30, 2002, \$18,258,246 in federal funds, and \$4,690,371 in state match had been disbursed, and \$17,402 was payable to borrowers.

Loans receivable as of June 30, 2002 are as follows:

<u>Loan Status</u>	<u>Loan Amount Authorized</u>	<u>Remaining Commitment</u>	<u>Loan Balance June 30, 2001</u>	<u>Loan Disbursements</u>	<u>Repayments and Principal Forgiveness</u>	<u>Loan Balance June 30, 2002</u>
Funding Completed	\$ 15,904,933	\$ -	\$ 10,817,380	\$ 3,297,439	\$ (694,055)	\$ 13,420,764
Funding in Progress	17,847,624	10,786,538	1,107,967	5,953,119	-	7,061,086
Total	\$ 33,752,557	10,786,538	\$ 11,925,347	\$ 9,250,558	\$ (694,055)	\$ 20,481,850

The Program made loans to nine local communities that totaled \$750,000 or more, and in the aggregate, exceeded \$15 million. The outstanding balances of these loans represent approximately 73 percent of the total loans outstanding as of June 30, 2002:

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Notes to Financial Statements

4. Loans Receivable (continued)

<u>Community</u>	<u>Loan Authorized</u>	<u>Loan Outstanding</u>
Berlin Water Works-01	\$ 1,553,708	\$ 1,475,966
Berlin Water Works-02	2,003,659	1,903,386
Berlin Water Works-03	794,621	784,845
Berlin Water Works-04	1,948,878	1,742,652
Hanover Water	4,035,000	3,989,783
Littleton Water & Light	750,000	750,000
City of Portsmouth	2,288,252	2,288,252
City of Portsmouth	889,545	889,545
Tilton	<u>1,293,694</u>	<u>1,228,614</u>
Subtotal \$750,000 or More	15,557,357	15,053,043
All other loans	<u>7,417,668</u>	<u>5,428,807</u>
Total Loans	<u>\$ 22,975,025</u>	<u>\$ 20,481,850</u>

Loans mature at various intervals through April, 2022. The scheduled principal and interest payments on completely disbursed loans maturing in the next five years and every five years thereafter are as follows:

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2003	\$ 897,760	\$ 341,515	\$ 1,239,275
2004	910,166	331,109	1,241,275
2005	850,413	312,731	1,163,144
2006	758,116	294,275	1,052,391
2007	681,663	275,856	957,519
2008-2012	3,394,290	1,097,770	4,492,060
2013-2017	3,430,845	619,245	4,050,090
2018-2022	<u>2,497,511</u>	<u>166,870</u>	<u>2,664,381</u>
Total	<u>\$13,420,764</u>	<u>\$ 3,439,371</u>	<u>\$16,860,135</u>

5. Contributed Capital

The Program is capitalized by grants through EPA. These grants have been awarded annually. The State of New Hampshire must also contribute an amount equal to 20 percent of the federal capitalization amount. The EPA grants and the State match are included in the net asset balance. New Hampshire's matching contribution has been provided through appropriation of State general fund resources and general obligation bonds of the State. As of June 30, 2002, EPA has awarded \$43,886,000 to the state, of which \$23,607,390 has been drawn for loans and set-aside expenses. The State has allocated match funds of \$8,777,200. The following summarizes the capitalization grant award, amounts drawn on each grant as of the balance sheet date, and balances available for future loans and set-aside costs:

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Notes to Financial Statements

6. Contributed Capital (continued)

Grant Amount	Total Draws as of June 30, 2001	2002 Draws	Total Draws as of June 30, 2002	Grant Funds Available June 30, 2002
\$ 13,754,800	\$ 13,109,239	\$ 305,477	\$ 13,414,716	\$ 340,084
7,121,300	1,097,191	5,543,437	6,640,628	480,672
7,463,800	149,276	2,711,306	2,860,582	4,603,218
7,757,000	60,369	362,785	423,154	7,333,846
7,789,100	-	268,310	268,310	7,520,790
<u>\$ 43,886,000</u>	<u>\$ 14,416,075</u>	<u>\$ 9,191,315</u>	<u>\$ 23,607,390</u>	<u>\$ 20,278,610</u>

As of June 30, 2001 and 2002, State matching contributions were as follows:

	<u>June 30, 2001</u>	<u>Contributions</u>	<u>June 30, 2002</u>
New Hampshire State Match	<u>\$ 2,812,023</u>	<u>\$ 1,878,348</u>	<u>\$ 4,690,371</u>

7. Set-Aside Costs

Total set-aside costs charged to the Program are as follows:

	Administrative Costs	Technical Assistance Costs	State Program Management Costs	Source Water Protection Costs	Total Set-Aside Costs
FY 1998	\$ 67,211	\$ 85,987	\$ 117,140	\$ 111,601	\$ 381,939
FY 1999	93,499	209,935	214,389	184,491	702,315
FY 2000	144,079	174,186	223,662	571,889	1,113,816
FY 2001	276,534	200,923	439,515	678,950	1,595,921
FY 2002	338,656	174,763	411,991	842,660	1,768,070
Total	<u>\$ 919,979</u>	<u>\$ 845,794</u>	<u>\$ 1,406,698</u>	<u>\$ 2,389,590</u>	<u>\$ 5,562,061</u>

8. Contingencies, Related Parties, and Subsequent Events

Contingencies

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

NEW HAMPSHIRE DEPARTMENT OF ENVIRONMENTAL SERVICES
Drinking Water State Revolving Fund
Notes to Financial Statements

8 Contingencies, Related Parties, and Subsequent Events (continued)

According to NHDES management and legal counsel, there are no other loss contingencies which require disclosure or accrual under the Statement of Financial Accounting Standards No. 5.

Related Parties

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

Subsequent Events

Subsequent to year end, the supplemental loan agreement (SLA) for Enfield was approved, and a principal forgiveness of \$47,693 was provided. In addition, while the SLAs were still pending, the Program estimated the allowable principal forgiveness for Berlin-03 and Berlin-04 by \$238,386 and \$584,663, respectively.

**Independent Auditor's Report on the
New Hampshire Drinking Water State Revolving Fund Program
Internal Control Structure Based on an
Audit of the Financial Statements
Performed in Accordance with
*Government Auditing Standards***



ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C

OFFICE OF
INSPECTOR GENERAL

Mr. Robert Monaco, Acting Commissioner
New Hampshire Department of Environmental Services

We have audited the financial statements of the New Hampshire Drinking Water State Revolving Fund Program (the Program) as of and for the year ended June 30, 2002, and have issued our report thereon dated October 11, 2002.

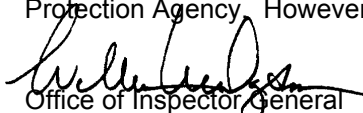
We conducted our audit in accordance with generally accepted auditing standards and *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The management of the Program is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the financial statements of the Program for the year ended June 30, 2002, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk 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 structure. Accordingly, we do not express such an opinion.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be material weaknesses under standards established by the American Institute of Certified Public Accountants. A material weakness is a condition in which the design or operation of one or more of the specific internal control elements does not reduce to a relatively low level the risk that errors and irregularities 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 structure and its operations that we consider to be material weaknesses as defined above.

This report is intended for the information of management of the Program and the U.S. Environmental Protection Agency. However, this report is a matter of public record and distribution is not limited.


Office of Inspector General
October 11, 2002

**Independent Auditor's Report
on Compliance with Requirements Applicable to the
New Hampshire Drinking Water State Revolving Fund Program
in Accordance with
*Government Auditing Standards***



ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C

OFFICE OF
INSPECTOR GENERAL

Mr. Robert Monaco, Acting Commissioner
New Hampshire Department of Environmental Services

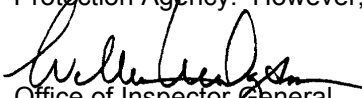
We have audited the financial statements of the New Hampshire Drinking Water State Revolving Fund Program (the Program) as of and for the year ended June 30, 2002, and have issued our report thereon dated October 11, 2002.

We have also audited the Program's compliance with 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, 2002. 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.

We conducted our audit of compliance in accordance with generally accepted auditing standards, *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 Program's compliance with those requirements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, except for matters discussed in the Findings and Recommendations Section, the Program complied, in all material respects, with the specific program requirements that are applicable to the Program for the year ended June 30, 2002.

This report is intended for the information of management of the Program and the U.S. Environmental Protection Agency. However, this report is a matter of public record and its distribution is not limited.


Office of Inspector General
October 11, 2002

Findings and Recommendations

State Match

As of June 30, 2002, DES had received \$111,345 in excess Federal funds and had a \$111,345 shortfall in State Funds required to be in the revolving loan fund. Per 40 CFR 35.3550(g), the State is to deposit 20 percent of each capitalization grant into the revolving loan fund. EPA's "Guide to Using EPA's Automated Clearing House for the Drinking Water State Revolving Fund Program" provided further details on how the state match should be provided. Per that guidance, the ratio of state match to total federal and state funds is calculated as follows:

State match ratio = State Match/(capitalization grant – set asides + state match)

Using this formula, the State should have deposited \$626,496 of state match and drawn \$2,599,960 in Federal Funds for project costs totaling \$3,226,456 being funded from the 1999 capitalization grant. The state had actually deposited \$515,151 in State match and drawn \$2,711,306 in Federal funds.

State Response

The state agreed with this condition and stated:

Since June 30, 2002, the state used additional state match on projects until the proper ratio of State match to Federal funds was achieved. The formula used to make draws has also been adjusted so that the proper ratio will be maintained in the future. The State wants to make it clear that the ratio that was formerly being used was the same formula mentioned in the above mentioned finding, the EPA document "Guide to Using EPA's Automated Clearing House for the Drinking Water State Revolving Fund Program" issued in September 1998. The misunderstanding is the interpretation of the way in which the formula was written. The State interpreted the formula to be based on federal dollars when in fact it was meant by EPA to be based on using total dollars.

Cost Allocation

The Water Supply Engineering Bureau's Administrator's salary and benefits were charged to the DWSRF's administration set-aside during the year, even though the Administrator oversees multiple drinking water programs and activities, such as enforcement, monitoring, operator certification, public water supply supervision, source water protection, and water management. The DWSRF administration set-aside is only to be used for administration of the DWSRF or technical assistance to public water systems. According to 40 CFR, Part 31 and OMB Circular A-87, distribution of salaries where employees work on multiple activities should be supported by personnel activity reports documenting the time spent working directly on the program or be allocated indirectly based upon a cost allocation methodology developed, documented, and maintained for audit. Assuming that the Administrator devotes 20 percent of his time working on DWSRF activities, approximately 4/5 of the costs charged to the DWSRF administration set aside, or approximately \$54,000 is questioned as ineligible.

State Response

The Administrator's salary and benefits has been changed and is now being charged to the "F" Set-Aside, State Program Management, and no more than 20% of his time will be allocated to the "D" Set-Aside, Administration. It is important to note that the Intended Use Plan submitted to EPA Region I was approved with the Administrator's salary being charged to administration.

Supplemental Information

State of New Hampshire
Drinking Water State Revolving Fund
Schedule of Set-aside Expenses
Year Ended June 30, 2002

<u>Description</u>	<u>Administration</u>	<u>Technical Assistance</u>	<u>State Program Management</u>	<u>Local Assistance</u>	<u>Total</u>
Payroll	\$ 204,882	\$ -	\$ 360,312	\$ 545,508	\$ 1,110,702
Contracts	6,848	174,763	-	37,030	218,641
Grants	-	-	-	149,226	149,226
Rent	40,208	-	-	-	40,208
Training	-	-	-	81,482	81,482
Equipment	-	-	6,044	13,971	20,015
Other Operating Costs	86,718	-	45,635	15,444	147,798
	<u>\$ 338,656</u>	<u>\$ 174,763</u>	<u>\$ 411,991</u>	<u>\$ 842,660</u>	<u>\$ 1,768,070</u>

**State of New Hampshire
Drinking Water State Revolving Fund
Supplemental Information**

Schedule of Loan Activity and Binding Commitments

Recipient	Project #	Total Original Loan		Construction	Return to	Principal	Principal	Amended	Remaining
		Commitment	Disbursements	Interest Added to Loan	Fund Balance	Payment Received	Forgiveness	Loans Outstanding	Loan Commitment
Bristol	0301010	\$ 153,356	\$ 138,253	\$ -	\$ 15,103	\$ 54,005	\$ 10,369	\$ 73,879	\$ -
Dover	0651010	250,000	250,000	-	-	204,702	-	45,298	-
Epping	0761010	550,000	538,056	-	11,944	27,420	-	510,636	-
Farmington	0811010	650,000	610,768	1,132	39,232	121,249	20,359	470,291	-
Greenville	0991010	1,425,000	1,276,940	-	148,060	1,276,940	-	-	-
Sunapee	2271010	644,074	356,242	508	287,832	139,360	26,718	190,671	-
Gunstock Village	0881020	112,000	52,000	-	60,000	20,432	-	31,568	-
Portsmouth	1951010-01	288,000	288,000	-	-	-	-	288,000	-
Portsmouth	1951020	360,000	123,102	-	236,898	123,102	-	-	-
Waterville Estates	0341020	28,170	6,916	-	21,254	6,916	-	-	-
Rockhouse Mountain	0512240	56,581	56,581	-	-	3,899	-	52,682	-
Tilton/Northfield	2351010	1,405,000	1,293,694	-	111,306	47,488	17,592	1,228,614	-
Hanover Water Works	1071010	4,035,000	4,035,000	-	-	45,217	-	3,989,783	-
Berlin	0231010-02	2,000,000	2,000,000	3,659	-	68,695	31,579	1,903,386	-
Berlin	0231010-01	1,550,000	1,550,000	3,708	-	53,268	24,474	1,475,966	-
Rosebrook Water Co.	0382010	120,000	120,000	-	-	10,398	-	109,602	-
Pennichuck Water Works	0612150	445,000	445,000	-	-	5,563	-	439,437	-
Town of Newport	1741010	553,403	553,403	-	-	108,083	20,753	424,567	-
Berlin Water Works	0231010-03	796,280	784,845	-	-	-	-	796,280	11,435
Berlin Water Works	0231010-04	2,010,000	1,742,652	-	-	-	-	2,010,000	267,348
City of Portsmouth	1951010-04	300,000	300,000	-	-	-	-	300,000	-
Walter Borowski	0043030	140,000	140,000	-	-	766	351	138,882	-
White Lake Estates	2312030	57,500	53,027	-	4,474	4,396	674	47,957	-
Town of Enfield	0751010	600,000	317,951	-	282,049	15,898	2,510	299,543	-
Town of Alton	0061010	550,000	262,492	-	-	-	-	550,000	287,508
Town of Raymond	1971010	1,500,000	78,385	-	-	-	-	1,500,000	1,421,615
Littleton Water & Light	1381010-01	750,000	750,000	-	-	-	-	750,000	-
City of Somersworth	2151010	650,000	650,000	-	-	-	-	650,000	-
City of Portsmouth	1951010-07	1,325,000	889,545	-	-	-	-	1,325,000	435,455
Jackson Water Precinct	1211010	1,800,000	250,274	-	-	-	-	1,800,000	1,549,726
City of Portsmouth	1951010-06	4,800,000	2,288,252	-	-	-	-	4,800,000	2,511,749
Town of Durham	0691010	900,000	540,680	-	-	-	-	900,000	359,320
Town of Meredith	1521010	850,344	2,743	-	-	-	-	850,344	847,601
Pennichuck Water Works	1932050	145,000	15,574	-	-	-	-	145,000	129,426
Evergreen Drive Water Corp	0262010	140,000	-	-	-	-	-	140,000	140,000
Berlin Water Works	0231010-05	2,000,000	188,241	-	-	-	-	2,000,000	1,811,759
City of Rochester	2001010-02	521,000	15,441	-	-	-	-	521,000	505,559
City of Rochester	2001010-01	510,000	1,961	-	-	-	-	510,000	508,040
Totals		\$ 34,970,708	\$ 22,966,018	\$ 9,007	\$ 1,218,151	\$ 2,337,796	\$ 155,379	\$ 31,268,388	\$ 10,786,538
Less remaining commitment, June 30, 2002								10,786,538	
Less Allowance for Principal Forgiveness								1,644,298	
Loans Receivable, June 30, 2002								\$ 18,837,552	

Report Distribution

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DWSRF Supervisor
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