

FINANCIAL AUDIT
INCLUDING THE PROVISIONS OF THE SINGLE AUDIT ACT
OF THE
DEPARTMENT OF ENVIRONMENTAL QUALITY

October 1, 1997 through September 30, 1999

EXECUTIVE DIGEST

DEPARTMENT OF ENVIRONMENTAL QUALITY

INTRODUCTION This report contains the results of our financial audit*, including the provisions of the Single Audit Act, of the Department of Environmental Quality (DEQ) for the period October 1, 1997 through September 30, 1999.

AUDIT PURPOSE This financial audit of DEQ was conducted as part of the constitutional responsibility of the Office of the Auditor General and is required on a biennial basis by Act 251, P.A. 1986, to satisfy the requirements of the Single Audit Act Amendments of 1996 and U.S. Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

BACKGROUND DEQ's mission* is to drive improvements in environmental quality for the protection of public health and natural resources to benefit current and future generations. This will be accomplished through effective administration of agency programs, providing for the use of innovative strategies, while helping to foster a strong and sustainable economy.

DEQ was created on August 1, 1995 by Executive Order 1995-18, which transferred environmental regulatory

* See glossary at end of report for definition.

programs from the Department of Natural Resources to the newly created DEQ. Subsequent executive orders impacting DEQ during our audit period included:

1. Executive Order 1998-2 transferred the remaining functions and responsibilities of the Above Ground Storage Tank Division from the Michigan Department of State Police to DEQ and created the Storage Tank Division.
2. Executive Order 1999-10 created the Water Quality Advisory Board, which was charged with advising DEQ regarding implementation of a comprehensive, long-term water quality monitoring program designed to measure the quality of Michigan's streams, rivers, and lakes and to detect areas of the State that need additional water quality control efforts.

DEQ's environmental program areas participate in managing federal grants. DEQ's financial and administrative functions are concentrated under the operations area.

DEQ's general operations are accounted for in the State's General Fund. DEQ administers environment related special revenue funds and an agency fund. As of September 30, 1999, DEQ had 1,577 employees and its General Fund expenditures and operating transfers out and special revenue fund expenditures were approximately \$201.2 million for fiscal year 1998-99.

**AUDIT OBJECTIVES
AND CONCLUSIONS**

Audit Objective: To audit DEQ's financial statements and schedules, including the schedule of expenditures of federal awards, as of and for the fiscal years ended September 30, 1999 and September 30, 1998.

Conclusion: We expressed an unqualified opinion* on DEQ's financial statements and schedules. In addition, we expressed an unqualified opinion on DEQ's supplemental financial statements and schedules, including the schedule of expenditures of federal awards, in relation to the financial statements and schedules taken as a whole.

Audit Objective: To assess and report on DEQ's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements and schedules, and on its internal control* over financial reporting, based on our audit of the financial statements and schedules.

Conclusion: Our assessment of compliance did not disclose any instances of noncompliance that could have a direct and material effect on the financial statements and schedules. Also, our assessment of internal control over financial reporting did not disclose any material weaknesses*. However, we identified reportable conditions* related to personnel and payroll functions and accounts payable estimation (Findings 1 and 2).

In addition, our assessment indicated that DEQ was in substantial compliance with the requirements set forth in Sections 18.1483 - 18.1487 of the *Michigan Compiled Laws* pertaining to its systems of internal accounting and administrative control.

Audit Objective: To assess and report on DEQ's compliance with requirements applicable to each major

* See glossary at end of report for definition.

federal program and on its internal control over compliance in accordance with OMB Circular A-133.

Conclusion: Our assessment of compliance applicable to each major federal program disclosed an instance of material noncompliance* related to State Revolving Fund* (SRF) Program* subrecipient designation (Finding 3) that is required to be reported under OMB Circular A-133:

- SRF Program subrecipient municipalities either did not submit Single Audit* reports or submitted reports that did not identify disbursements received from SRF as federal financial assistance on their schedules of expenditures of federal awards.

However, our assessment of internal control over compliance applicable to each major federal program did not disclose any material weaknesses. We did identify reportable conditions related to federal grant payroll cost allocation and personnel and payroll functions (Findings 4 and 5).

**AUDIT SCOPE AND
METHODOLOGY**

Our audit scope was to examine the financial and other records of the Department of Environmental Quality for the period October 1, 1997 through September 30, 1999. Our audit was conducted in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and, accordingly, included such tests of the records and such

* See glossary at end of report for definition.

other auditing procedures as we considered necessary in the circumstances.

**AGENCY RESPONSES
AND PRIOR AUDIT
FOLLOW-UP**

Our audit report contains 4 findings and 8 corresponding recommendations. DEQ's corrective action plan indicates that it agrees with 3 recommendations, agrees in part with 2 recommendations, and disagrees with 3 recommendations.

As disclosed in DEQ's summary schedule of prior audit findings, DEQ indicated that it fully corrected 10 of the 11 prior Single Audit findings and did not correct the remaining finding. However, 4 prior audit recommendations are repeated in this report (see Findings 1, 3, and 4).

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November 22, 2000

Mr. Russell J. Harding, Director
Department of Environmental Quality
Hollister Building
Lansing, Michigan

Dear Mr. Harding:

This is our report on the financial audit, including the provisions of the Single Audit Act, of the Department of Environmental Quality for the period October 1, 1997 through September 30, 1999.

This report contains our executive digest; description of agency; audit objectives and conclusions, audit scope, and agency responses and prior audit follow-up; schedule of findings and questioned costs; and independent auditor's reports on the financial statements, on the financial schedules, on compliance and on internal control over financial reporting, and on compliance with requirements applicable to each major program and on internal control over compliance in accordance with U.S. Office of Management and Budget Circular A-133. This report also contains the Department of Environmental Quality financial statements and schedules and notes to the financial statements and schedules, supplemental financial statements and schedules, other schedules, and a glossary of acronyms and terms.

Our findings and recommendations are organized by audit objective. The agency preliminary responses are contained in the corrective action plan. The *Michigan Compiled Laws* and administrative procedures require that the audited agency develop a formal response within 60 days after release of the audit report.

We appreciate the courtesy and cooperation extended to us during this audit.

AUDITOR GENERAL

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Description of Agency

The Department of Environmental Quality's (DEQ's) mission is to drive improvements in environmental quality for the protection of public health and natural resources to benefit current and future generations. This will be accomplished through effective administration of agency programs, providing for the use of innovative strategies, while helping to foster a strong and sustainable economy.

DEQ was created on August 1, 1995 by Executive Order 1995-18, which transferred environmental regulatory programs from the Department of Natural Resources to the newly created DEQ. Subsequently, the following executive orders transferred additional responsibilities to DEQ:

1. Executive Order 1996-1 transferred responsibilities for environmental health programs relating to drinking water and radiological protection from the Department of Public Health (now known as the Department of Community Health) to DEQ.
2. Executive Order 1996-2 transferred the Low-Level Radioactive Waste Authority from the Department of Commerce (now known as the Department of Consumer and Industry Services) to DEQ.
3. Executive Order 1997-2 transferred the Above Ground Storage Tank Program and the inspection of dry cleaning establishments from the Fire Marshal Division of the Michigan Department of State Police to DEQ.
4. Executive Order 1997-3 transferred the Michigan Environmental Science Board and the Environmental Administration Division from the Department of Management and Budget to DEQ.
5. Executive Order 1998-2 transferred the remaining functions and responsibilities of the Above Ground Storage Tank Division from the Michigan Department of State Police to DEQ and created the Storage Tank Division.

6. Executive Order 1999-10 created the Water Quality Advisory Board, which was charged with advising DEQ regarding implementation of a comprehensive, long-term water quality monitoring program designed to measure the quality of Michigan's streams, rivers, and lakes and to detect areas of the State that need additional water quality control efforts.

DEQ's environmental program areas participate in managing federal grants, including applying for grants, approving expenditures, and monitoring compliance with grant program requirements. Each program area is headed by a division chief who reports directly to the DEQ director. Under the program areas, district and other field offices are located Statewide.

DEQ's financial and administrative functions are concentrated under the operations area. Various administrative and general support functions, such as internal audit, personnel, budget, accounting, federal grant reporting, procurement, automation coordination, field operations coordination, and special environmental projects, are conducted under this area.

DEQ's general operations are accounted for in the State's General Fund. DEQ administers environment related special revenue funds and an agency fund. As of September 30, 1999, DEQ had 1,577 employees, and its General Fund expenditures and operating transfers out and special revenue fund expenditures were approximately \$201.2 million for fiscal year 1998-99.

Audit Objectives and Conclusions, Audit Scope,
and Agency Responses and Prior Audit Follow-Up

Audit Objectives and Conclusions

Our financial audit, including the provisions of the Single Audit Act, of the Department of Environmental Quality (DEQ) had the following objectives:

1. To audit DEQ's financial statements and schedules, including the schedule of expenditures of federal awards, as of and for the fiscal years ended September 30, 1999 and September 30, 1998.

We expressed an unqualified opinion on DEQ's financial statements and schedules. In addition, we expressed an unqualified opinion on DEQ's supplemental financial statements and schedules, including the schedule of expenditures of federal awards, in relation to the financial statements and schedules taken as a whole.

2. To assess and report on DEQ's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the financial statements and schedules, and on its internal control over financial reporting, based on our audit of the financial statements and schedules.

Our assessment of compliance did not disclose any instances of noncompliance that could have a direct and material effect on the financial statements and schedules. Also, our assessment of internal control over financial reporting did not disclose any material weaknesses. However, we identified reportable conditions related to personnel and payroll functions and accounts payable estimation (Findings 1 and 2).

In addition, our assessment indicated that DEQ was in substantial compliance with the requirements set forth in Sections 18.1483 - 18.1487 of the *Michigan Compiled Laws* pertaining to its systems of internal accounting and administrative control.

The findings related to our assessment of compliance and internal control over financial reporting are contained in Section II of the schedule of findings and questioned costs*.

3. To assess and report on DEQ's compliance with requirements applicable to each major federal program and on its internal control over compliance in accordance with U.S. Office of Management and Budget (OMB) Circular A-133.

Our assessment of compliance applicable to each major federal program disclosed an instance of material noncompliance related to State Revolving Fund (SRF) Program subrecipient designation (Finding 3) that is required to be reported under OMB Circular A-133. SRF Program subrecipient municipalities either did not submit Single Audit reports or submitted reports that did not identify disbursements received from SRF as federal financial assistance on their schedules of expenditures of federal awards.

However, our assessment of internal control over compliance applicable to each major federal program did not disclose any material weaknesses. We did identify reportable conditions related to federal grant payroll cost allocation and personnel and payroll functions (Findings 4 and 5).

The findings related to our assessment of compliance and internal control over compliance applicable to each major federal program are contained in Section III of the schedule of findings and questioned costs.

Audit Scope

Our audit scope was to examine the financial and other records of the Department of Environmental Quality for the period October 1, 1997 through September 30, 1999. Our audit was conducted in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and, accordingly, included such tests of the records and such other auditing procedures as we considered necessary in the circumstances.

* See glossary at end of report for definition.

We considered DEQ's internal control over compliance applicable to each major federal program and assessed DEQ's compliance with federal laws and regulations in accordance with the Single Audit Act Amendments of 1996 and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, in addition to generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. In addition, we followed up on DEQ's summary schedule of prior audit findings. DEQ's major federal programs are identified in Section I of the schedule of findings and questioned costs.

Agency Responses and Prior Audit Follow-Up

Our audit report contains 4 findings and 8 corresponding recommendations. DEQ's corrective action plan indicates that it agrees with 3 recommendations, agrees in part with 2 recommendations, and disagrees with 3 recommendations.

DEQ's corrective action plan, which is included in this report, was prepared by DEQ as required by OMB Circular A-133. Section 18.1462 of the *Michigan Compiled Laws* and Department of Management and Budget Administrative Guide procedure 1280.02 require DEQ to develop a formal response to our audit findings and recommendations within 60 days after release of the audit report.

As disclosed in DEQ's summary schedule of prior audit findings, DEQ indicated that it fully corrected 10 of the 11 prior Single Audit findings and did not correct the remaining finding. However, 4 prior audit recommendations are repeated in this report (see Findings 1, 3, and 4).

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

Section I: Summary of Auditor's Results

Financial Statements and Schedules

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weaknesses identified? No

Reportable conditions identified that are not considered to be material weaknesses? Yes

Noncompliance material to the financial statements and schedules? No

Federal Awards

Internal control over major programs:

Material weaknesses identified? No

Reportable conditions identified that are not considered to be material weaknesses? Yes

Type of auditor's report issued on compliance for major programs:
Unqualified for all major programs except for Capitalization Grants for State Revolving Funds, which is qualified*.

Any audit findings disclosed that are required to be reported in accordance with U.S. Office of Management and Budget (OMB) Circular A-133, Section 510(a)? Yes

* See glossary at end of report for definition.

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program</u>
66.419	Water Pollution Control - State and Interstate Program Support
66.458	Capitalization Grants for State Revolving Funds
66.468	Capitalization Grants for Drinking Water State Revolving Funds
66.805	Leaking Underground Storage Tank Trust Fund Program

Dollar threshold used to distinguish between type A and type B programs: \$3,000,000

Auditee qualified as a low-risk auditee*? No

Section II: Findings Related to the Financial Statements and Schedules

FINDING (760001)

1. Personnel and Payroll Functions

The Department of Environmental Quality (DEQ) had not developed and implemented effective internal control for personnel and payroll functions. Management controls are critical to help prevent and detect, on a timely basis, the processing of erroneous and unauthorized transactions.

* See glossary at end of report for definition.

Our review of personnel and payroll functions disclosed the following internal control weaknesses:

- a. DEQ did not consistently prepare and reconcile daily transaction control logs of transactions entered into the Personnel-Payroll Information System for Michigan (PPRISM).

To help ensure that transactions were properly entered and to disclose any unauthorized transactions, PPRISM Procedures Manual section 2.3 requires agencies to complete a department/agency daily transaction control log of transactions entered into PPRISM and then reconcile this daily log with the number of transactions shown as entered on the daily transaction control count.

DEQ did not implement procedures to ensure that the department/agency daily transaction control logs were prepared and reconciled with the daily transaction control count. Without such procedures, DEQ lacked assurance that payroll transactions entered into PPRISM were properly authorized and recorded.

In response to a similar finding in our prior audit report, DEQ stated that, as of August 1998, the Office of Personnel Services implemented a process whereby a supervisor generated the department/agency daily transaction control logs and reconciled the number of transactions entered with the daily transaction control count. However, our follow-up of five subsequent pay periods disclosed that DEQ prepared only one department/agency daily transaction control log.

- b. DEQ did not separate payroll duties between the transaction operators and the agency master operator.

To ensure that only authorized individuals have access to PPRISM, PPRISM Procedures Manual section 2.1 states that only the agency master operator should have the capacity to establish a new operator, inactivate an operator, or change operator capabilities. PPRISM transaction operators had both

transaction input capabilities and the ability to establish or change operator capabilities.

DEQ allowed three transaction operators to have the capability to establish a new operator, inactivate an operator, or change operator capabilities. As a result, DEQ lacked the assurance that only authorized individuals had access to PPRISM.

In response to a similar finding in our prior audit, DEQ stated that, although the transaction operators have the ability to establish or change operator capabilities, DEQ uses compensating controls to monitor activity. DEQ stated that the "CNTL* code" was implemented in August 1998 and is now used to daily review the instances of "PSWU* code" use, and the State of Michigan PPRISM valid operators report (CR-185) is monitored to review current users and their status. However, as noted in item a., DEQ did not consistently prepare and reconcile daily control logs of transactions entered into PPRISM to ensure that all transactions were properly entered and authorized.

- c. DEQ's internal control did not detect transaction operators who entered their own PPRISM transactions or prevent them from doing so. We identified two transaction operators who entered transactions for themselves. One operator had the capability to change pay range, step and rate, standard hours, and deferred hours. The second operator had the capability to change standard payroll distribution and gross pay adjustments. These capabilities could allow an operator to bypass essential controls, such as proper separation of duties.
- d. DEQ did not reconcile the PPRISM biweekly transaction reports (PE-110 reports) with source documents.

Reconciliation of the PE-110 reports with source documents by a control person who does not have the capability to process PPRISM transactions would help ensure that transactions are accurately processed. DEQ had not prepared reconciliations for the four PE-110 reports that we reviewed.

** See glossary at end of report for definition.*

RECOMMENDATIONS

- (a) WE AGAIN RECOMMEND THAT DEQ CONSISTENTLY PREPARE AND RECONCILE DAILY TRANSACTION CONTROL LOGS OF TRANSACTIONS ENTERED INTO PPRISM.

- (b) WE AGAIN RECOMMEND THAT DEQ SEPARATE PAYROLL DUTIES BETWEEN THE TRANSACTION OPERATORS AND THE AGENCY MASTER OPERATOR.

- (c) We recommend that DEQ develop and implement effective management controls to detect and help prevent transaction operators from entering their own PPRISM transactions.

- (d) We recommend that DEQ reconcile the PE-110 reports with source documents.

FINDING (760002)

2. Accounts Payable Estimation

The Drinking Water and Radiological Protection Division (DWRPD) did not develop a method for estimating fiscal year-end accounts payable. As a result, expenditures and accounts payable in the Combined Environmental Protection Bond Fund and the Bottle Deposits Fund were misstated.

DEQ's financial statements contained in this report are prepared on the modified accrual basis of accounting, as provided by generally accepted accounting principles and the Department of Management and Budget. The modified accrual basis of accounting emphasizes the measurement of current financial resources and obligations. Thus, an expenditure is recorded when a liability is incurred.

DWRPD had not estimated the amounts due to vendors at the close of the fiscal year. DWRPD recorded invoices as expenditures in the new fiscal year even though services were provided in the old fiscal year.

In our expenditure testing, we reviewed nine vouchers totaling \$1,248,889 for DWRPD for two fiscal years. We found one voucher for the Combined Environmental Protection Bond Fund that included \$350,567 that was recognized as a fiscal year 1997-98 expenditure. However, this expenditure should have been recorded as an account payable and recognized as an expenditure for fiscal year 1996-97. We also found one fiscal year 1998-99 voucher for the Bottle Deposits Fund that included \$23,390 that should have been recorded as accounts payable and recognized as fiscal year 1997-98 expenditures. The vouchers related to activities performed at workproject sites administered by DWRPD.

RECOMMENDATION

We recommend that DWRPD develop a method for estimating fiscal year-end accounts payable.

The status of the findings reported in the prior Single Audit is disclosed in the summary schedule of prior audit findings.

Section III: Findings and Questioned Costs Related to Federal Awards

FINDING (760003)

3. State Revolving Fund (SRF) Program Subrecipient Designation

U.S. Environmental Protection Agency	CFDA: 66.458 Capitalization Grants for State Revolving Funds
Award Numbers: CS260001-95, CS260001-96, CS260001-97, CS260001-98, CS260001-99	Award Period: 10/1/97 - 9/30/99
	Questioned Costs: \$0

U.S. Environmental Protection Agency	CFDA: 66.468 Capitalization Grants for Drinking Water State Revolving Funds
Award Numbers: FS985747-01 and FS995500-01	Award Period: 10/1/97 - 9/30/99
	Questioned Costs: \$0

SRF Program subrecipient municipalities either did not submit Single Audit reports or submitted reports that did not identify disbursements received from SRF as federal financial assistance on their schedules of expenditures of federal awards. This indicates that the municipalities' use of SRF money was not subject to audit testing for compliance with applicable federal program laws and regulations.

DEQ and the Michigan Municipal Bond Authority (MMBA), Department of Treasury, administer the SRF Program and the Drinking Water State Revolving Fund* (DWSRF) Program*, with DEQ as the direct recipient of the federal Capitalization Grants for State Revolving Funds (CFDA #66.458) and the Capitalization Grants for Drinking Water State Revolving Funds (CFDA #66.468). Subrecipient project eligibility and loan terms are determined by DEQ. Loan processing and actual distribution of funds to subrecipient municipalities from SRF and DWSRF are directed by MMBA. The sources of funds within SRF and DWSRF from which municipalities draw assistance include federal SRF and DWSRF Capitalization Grants, repayments of prior loan principal and interest, and SRF and DWSRF earnings.

Our review of 38 SRF loans, which met the Single Audit threshold, to 27 municipalities disclosed that 4 municipalities did not submit Single Audit reports. Also, 29 Single Audit reports did not identify disbursements received from SRF as federal assistance on their schedules of expenditures of federal awards. None of the DWSRF loans to municipalities met the Single Audit threshold.

The U.S. Environmental Protection Agency's (EPA's) SRF and DWSRF Program Guidance states that the direct recipient of the federal assistance (i.e., DEQ) must ensure that the SRF and DWSRF Program subrecipients comply with the provisions of the Single Audit Act. Also, this guidance states that funds directly made available to the municipalities from the SRF and DWSRF Capitalization Grants should be considered federal funds subject to the terms of the Single Audit Act. Further, Title 40, Part 31, section 37 of the *Code of Federal Regulations* requires DEQ to ensure that its subrecipients are aware of requirements imposed upon them by federal statute and regulations. In addition, the Single Audit Act requires DEQ to provide subrecipients with the federal program name and

* See glossary at end of report for definition.

identifying numbers in addition to the federal requirements which govern the use of awards.

Without Single Audit reports and clear identification to SRF and DWSRF Program subrecipient municipalities that SRF and DWSRF loans are federal financial assistance, DEQ does not have assurance that the municipalities are complying with all federal regulations applicable to the SRF and DWSRF Programs. Although the receipt of audit reports does not by itself constitute effective subrecipient monitoring, the reports identify internal control weaknesses and instances of noncompliance with laws and regulations that need additional follow-up by DEQ. DEQ reported distributions to subrecipients of \$89.0 million and \$73.6 million in fiscal years 1997-98 and 1998-99, respectively, for Capitalization Grants for State Revolving Funds on its schedule of expenditures of federal awards. DEQ also reported distributions to subrecipients of \$1.6 million and \$31.4 million in fiscal years 1997-98 and 1998-99, respectively, for Capitalization Grants for Drinking Water State Revolving Funds on its schedule of expenditures of federal awards.

In its response to a similar prior audit finding, DEQ stated that it disagreed with the finding as confusion has existed within the State and across the country over the nature of these funds. Also, MMBA has stated that it did not consider SRF and DWSRF loans to municipalities to be federal financial assistance. DEQ could obtain resolution of this conflict by requesting the EPA to formally rule on whether SRF and DWSRF loans to municipalities constitute federal financial assistance.

RECOMMENDATIONS

WE AGAIN RECOMMEND THAT DEQ ENSURE THAT SRF PROGRAM SUBRECIPIENT MUNICIPALITIES ARE AWARE THAT SRF LOANS ARE FEDERAL FINANCIAL ASSISTANCE BY REQUIRING THESE MUNICIPALITIES TO SUBMIT SINGLE AUDIT REPORTS IDENTIFYING DISBURSEMENTS RECEIVED FROM SRF AS FEDERAL FINANCIAL ASSISTANCE ON THEIR SCHEDULES OF EXPENDITURES OF FEDERAL AWARDS.

We also recommend that DEQ request the EPA to formally rule on whether SRF and DWSRF loans to municipalities constitute federal financial assistance.

FINDING (760004)

4. Federal Grant Payroll Cost Allocation

U.S. Environmental Protection Agency	<i>CFDA</i> : 66.419 Water Pollution Control - State and Interstate Program Support
Award Numbers: M005260-98 and M006260-99	Award Period: 10/1/97 - 9/30/99
	Questioned Costs: \$0

U.S. Environmental Protection Agency	<i>CFDA</i> : 66.458 Capitalization Grants for State Revolving Funds
Award Numbers: CS260001-95, CS260001-96, CS260001-97, CS260001-98, CS260001-99	Award Period: 10/1/97 - 9/30/99
	Questioned Costs: \$538,863

DEQ had not established a system to properly allocate payroll expenditures to all federal grant programs.

OMB Circular A-87, Attachment B, requires that employees maintain personnel activity reports to support charges to federal grants. This regulation allows the use of estimates and other methods for interim accounting. However, at least quarterly, comparisons of actual costs with budget distributions are required to be completed and adjustments made as required.

Our review of payroll expenditures charged to federal grant programs disclosed:

- a. The Surface Water Quality Division charged payroll costs to the Water Pollution Control - State and Interstate Program Support grant (*CFDA* #66.419) on a budget-driven estimation basis without performing quarterly reconciliations. Employees maintained biweekly personnel activity logs; however, some of these logs were not used to bill the federal program or to reconcile the estimations. Some payroll charges were based on managers' predictions made at the beginning of the fiscal year of work estimates to be performed by their employees. DEQ budget personnel concurred with our observations related to such allocations. Because of a lack of documentation

to support DEQ's payroll allocation, we could not quantify the questioned costs associated with this error.

The Division's improper basis for allocation of payroll expenditures may have contributed to its underutilization of federal funds. We determined that DEQ could have received an additional \$9,672 and \$43,128 for fiscal years 1997-98 and 1998-99, respectively. DEQ personnel informed us that improved communication among division personnel and full utilization of the State's Data Collection and Distribution System (DCDS) are inherent components of an effective payroll allocation methodology, thus helping to prevent undercapitalization of federal funds.

- b. The Environmental Assistance Division allocated administrative staff costs to SRF on a budgeted basis rather than according to actual time worked or another allowable allocation methodology. Prior to fiscal year 1998-99, all administrative staff costs were charged to SRF. During fiscal year 1998-99, the Division revised the allocation and charged administrative staff costs 50% to SRF and 50% to the Waste Reduction Fees Fund. The percentages charged to SRF were based solely on the budgeted basis and were not supported by an allowable allocation methodology.

During fiscal years 1998-99 and 1997-98, the Division allocated administrative staff costs to SRF of \$224,329 and \$314,534, respectively.

In response to a similar finding in our prior audit report, DEQ stated that it would implement steps to ensure that charges to the federal grants would reflect actual work records and personnel activity reports. During our audit fieldwork, DEQ informed us that it has implemented corrective action for fiscal year 1999-2000.

RECOMMENDATION

WE AGAIN RECOMMEND THAT DEQ ESTABLISH A SYSTEM TO PROPERLY ALLOCATE PAYROLL EXPENDITURES TO ALL FEDERAL GRANT PROGRAMS.

FINDING (760005)

5. Personnel and Payroll Functions

Applicable to: All federal programs

This finding is included in Section II of the schedule of findings and questioned costs (760001).

The status of the findings reported in the prior Single Audit is disclosed in the summary schedule of prior audit findings.

Independent Auditor's Report on
the Financial Statements

August 25, 2000

Mr. Russell J. Harding, Director
Department of Environmental Quality
Hollister Building
Lansing, Michigan

Dear Mr. Harding:

We have audited the accompanying combined balance sheet of the Department of Environmental Quality as of September 30, 1999 and September 30, 1998 and the related combined statement of revenues, expenditures, and changes in fund balances for the fiscal years then ended. These financial statements are the responsibility of the Department'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 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 the 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 described in Note 1d, the accompanying financial statements include only specific funds administered by the Department of Environmental Quality. Accordingly, these financial statements are not intended to present fairly the financial position and results of operations of the Department, the State of Michigan, or the State's special revenue and agency funds.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the Department of Environmental Quality's funds, as listed in Note 1a, as of September 30, 1999 and September 30, 1998 and the results of operations for the fiscal years then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 25, 2000 on our tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grants and on our consideration of its internal control over financial reporting.

The accompanying supplemental financial statements, as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the Department's financial statements referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

AUDITOR GENERAL

Independent Auditor's Report on
the Financial Schedules

August 25, 2000

Mr. Russell J. Harding, Director
Department of Environmental Quality
Hollister Building
Lansing, Michigan

Dear Mr. Harding:

We have audited the accompanying schedule of General Fund revenues and operating transfers and the schedule of sources and disposition of General Fund authorizations of the Department of Environmental Quality for the fiscal years ended September 30, 1999 and September 30, 1998. These financial schedules are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial schedules based on our audit. The governmental operations of the Department are accounted for principally in the General Fund of the State of Michigan.

We conducted our audit in accordance with generally accepted auditing standards 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 schedules are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial schedules. An audit also includes assessing the accounting principles used and the significant estimates made by management, as well as evaluating the overall financial schedule presentation. We believe that our audit provides a reasonable basis for our opinion.

As described in Note 1d, the accompanying financial schedules include only the revenues and operating transfers and the sources and disposition of authorizations for the Department of Environmental Quality's General Fund accounts, presented on the modified accrual basis of accounting. Accordingly, these financial schedules are not intended to constitute a complete financial presentation of either the Department or the State's General Fund in accordance with generally accepted accounting principles.

In our opinion, the financial schedules referred to in the first paragraph present fairly, in all material respects, the revenues and operating transfers and the sources and disposition of authorizations of the Department of Environmental Quality for the fiscal years ended September 30, 1999 and September 30, 1998 on the basis of accounting described in Note 1c.

In accordance with *Government Auditing Standards*, we have also issued a report dated August 25, 2000 on our tests of the Department's compliance with certain provisions of laws, regulations, contracts, and grants and on our consideration of its internal control over financial reporting.

The accompanying schedule of expenditures of federal awards, required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the Department's financial schedules referred to in the first paragraph. Such information has been subjected to the auditing procedures applied in the audit of the financial schedules and, in our opinion, is fairly stated, in all material respects, in relation to the financial schedules taken as a whole.

AUDITOR GENERAL

Independent Auditor's Report on Compliance and
on Internal Control Over Financial Reporting

August 25, 2000

Mr. Russell J. Harding, Director
Department of Environmental Quality
Hollister Building
Lansing, Michigan

Dear Mr. Harding:

We have audited the financial statements and schedules of the Department of Environmental Quality as of and for the fiscal years ended September 30, 1999 and September 30, 1998 and have issued our reports thereon dated August 25, 2000. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Department's financial statements and schedules are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement and schedule 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 that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Department'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 schedules and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to

our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Department's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements and schedules. Reportable conditions are described in the accompanying schedule of findings and questioned costs as Findings 1 and 2.

A material weakness is a 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 in amounts that would be material in relation to the financial statements and/or schedules being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. 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 reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that neither of the reportable conditions described in the previous paragraph is a material weakness.

This report is intended solely for the information and use of the State's management, the Legislature, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

Independent Auditor's Report on Compliance With
Requirements Applicable to Each Major Program
and on Internal Control Over Compliance in
Accordance With OMB Circular A-133

August 25, 2000

Mr. Russell J. Harding, Director
Department of Environmental Quality
Hollister Building
Lansing, Michigan

Dear Mr. Harding:

Compliance

We have audited the compliance of the Department of Environmental Quality with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement that are applicable to each major federal program for the fiscal years ended September 30, 1999 and September 30, 1998. The Department's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each major federal program is the responsibility of the Department's management. Our responsibility is to express an opinion on the Department's compliance based on our audit.

We conducted our audit of compliance in accordance with generally accepted auditing standards; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to in the previous paragraph that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Department'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 Department's compliance with those requirements.

As described in Finding 3 in the accompanying schedule of findings and questioned costs, the Department did not comply with requirements regarding subrecipient monitoring that are applicable to its State Revolving Fund Program. Compliance with such requirements is necessary, in our opinion, for the Department to comply with the requirements applicable to that program.

In our opinion, except for the noncompliance described in the previous paragraph, the Department of Environmental Quality complied, in all material respects, with the requirements referred to in the third previous paragraph that are applicable to each major federal program for the fiscal years ended September 30, 1999 and September 30, 1998.

Internal Control Over Compliance

The management of the Department is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Department's internal control over compliance with requirements that could have a direct and material effect on a major federal program 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 OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the Department's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. Reportable conditions are described in the accompanying schedule of findings and questioned costs as Findings 4 and 5.

A material weakness is a 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 applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major 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. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe

that neither of the reportable conditions described in the previous paragraph is a material weakness.

This report is intended solely for the information and use of the State's management, the Legislature, federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

AUDITOR GENERAL

Description of Special Revenue Funds

COMBINED ENVIRONMENTAL PROTECTION BOND FUND

This Fund, which is administered by the Department of Environmental Quality (DEQ), was established by Act 328, P.A. 1988, to account for the proceeds of \$660 million of general obligation bonds approved by Michigan voters in November 1988. The bonds are authorized for financing environmental protection programs to clean up sites of toxic and other environmental contamination and contribute to a regional Great Lakes Protection Fund; address solid waste problems; treat sewage and other water quality problems; and reuse industrial sites and preserve open space. The Act also specifies that not more than \$425 million of the proceeds of these bonds be available to clean up sites of toxic and other environmental contamination; not more than \$150 million be available for solid waste projects; not more than \$60 million be available to capitalize the State Water Pollution Control Loan Fund (recorded as equity transfers to the Michigan Municipal Bond Authority); and not more than \$25 million be available to fund Michigan's participation in a regional Great Lakes Protection Fund.

Act 284, P.A. 1998, expanded this Fund to account for the proceeds of \$570 million of general obligation bonds approved by Michigan voters in November 1998. Act 288, P.A. 1998, directs that not more than \$335 million can be used for environmental response activities at facilities; not more than \$50 million for waterfront improvements; not more than \$25 million for remediation of contaminated lake and river sediments; not more than \$50 million for nonpoint source pollution prevention and control projects or wellhead protection projects; not more than \$90 million for water quality monitoring and water resources protection and pollution control activities; and not more than \$20 million for pollution prevention programs.

MICHIGAN UNDERGROUND STORAGE TANK FINANCIAL ASSURANCE (MUSTFA) FUND

The MUSTFA Fund was established by Act 518, P.A. 1988, to assist certain owners and operators of underground storage tank systems in meeting their financial responsibility requirements provided for in the Solid Waste Disposal Act. It is administered by DEQ and an 11-member advisory board.

The primary source of revenues is an environmental protection regulatory fee of 7/8 of a cent per gallon imposed on all refined petroleum products sold for resale. Expenditures are primarily amounts spent to assist in environmental clean-up. Acts 252 and 269, P.A. 1995, limit the MUSTFA Fund's liability for claims to those billings received by June 29, 1995. The State's liability for environmental cleanup claims is further limited by law to the amount of available resources. Liabilities, in excess of available funds, for unpaid work performed on eligible environmental cleanup claims will be paid from future years' revenues and are recorded as a liability in the general long-term obligations account group.

BOTTLE DEPOSITS FUND

This Fund was created by Act 384, P.A. 1996, to provide for the disposition of unredeemed bottle deposits. The Fund is jointly administered by the Department of Treasury and DEQ. The law mandates that, when the Fund is operational, an annual distribution of the funds will be made as follows: 25% returned to the dealers and 75% to fund several subfunds.

The 75% is initially deposited into the Cleanup and Redevelopment Trust Subfund (CRTF) and, if not further distributed, remains there until the principal amount reaches \$200 million. In the first year of operations, the \$35 million of bottle deposits arrearage revenues were applied to CRTF. For each of the fiscal years 1996-97, 1997-98, and 1998-99, up to \$15 million must be distributed from CRTF to the Cleanup and Redevelopment Subfund (CRF). Additionally, of funds received annually by CRTF, 80% is allocated to CRF and 10% to the Community Pollution Prevention Subfund.

Act 380, P.A. 1996, moved the former Environmental Response Fund (ERF) to a subfund of CRF. The law mandates that proceeds of all cost recovery actions taken and settlements entered into pursuant to ERF (excluding natural resource damages) by DEQ or the Attorney General, or both, shall be credited to ERF.

Description of Agency Fund

ENVIRONMENTAL QUALITY DEPOSITS FUND

This Fund was reauthorized by Act 451, P.A. 1994, as amended, to account for cash bonds posted by applicants desiring licenses to operate hazardous and solid waste disposal areas. Because the Scrap Tire Regulatory Fund created by Act 451, P.A. 1994, has similar provisions, both of these activities are accounted for in this Fund. In accordance with Act 451, P.A. 1994, as amended, interest earnings at an annual rate of 6% are credited to the applicant's account. This Act also specifies the circumstances under which the director of the Department of Environmental Quality is authorized to use the deposits to close and maintain a facility or return the deposit upon the operator's satisfactory closure and maintenance of the facility.

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
 Combined Balance Sheet
 As of ~~September 30~~
 (in thousands)

	<u>Governmental Fund Types</u>		<u>Fiduciary Fund Types</u>	
	<u>Special Revenue</u>		<u>Agency</u>	
	<u>1999</u>	<u>1998</u>	<u>1999</u>	<u>1998</u>
ASSETS				
Current Assets:				
Cash	\$ 46	\$ 81	\$	\$
Equity in Common Cash	139,506	179,354	3,371	3,695
Taxes, interest, and penalties receivable	4,855	5,107		
Amounts due from other funds	15,248	1,055		
Amounts due from local units	30			
Other current assets	<u>1,427</u>	<u>2,573</u>		
Total Current Assets	\$ 161,112	\$ 188,170	\$ 3,371	\$ 3,695
Amounts due from local units	1,330			
Other noncurrent assets	<u>1,411</u>	<u>2,172</u>		
Total Assets	<u>\$ 163,853</u>	<u>\$ 190,342</u>	<u>\$ 3,371</u>	<u>\$ 3,695</u>
LIABILITIES AND FUND BALANCES				
Current Liabilities:				
Warrants outstanding	\$ 2,299	\$ 1,244	\$	\$
Accounts payable and other liabilities	26,494	23,423	3,371	3,695
Amounts due to other funds	18,126	39,550		
Deferred revenue	<u>433</u>	<u>472</u>		
Total Current Liabilities	\$ 47,352	\$ 64,689	\$ 3,371	\$ 3,695
Deferred revenue	<u>1,352</u>	<u>1,954</u>		
Total Liabilities	<u>\$ 48,704</u>	<u>\$ 66,643</u>	<u>\$ 3,371</u>	<u>\$ 3,695</u>
Fund Balances:				
Reserves for:				
Budgetary carry-forwards:				
Encumbrances	\$ 4,226	\$ 5	\$	\$
Restricted revenues	71,053	58,830		
Multi-year projects	61,486	75,278		
Revolving loan programs	2,670			
Funds held as permanent investments (Note 7)	2,900	1,775		
Noncurrent assets	<u>1,389</u>			
Total Reserved	\$ 143,724	\$ 135,888	\$ 0	\$ 0
Unreserved	<u>(28,575)</u>	<u>(12,189)</u>		
Total Fund Balances	<u>\$ 115,149</u>	<u>\$ 123,699</u>	<u>\$ 0</u>	<u>\$ 0</u>
Total Liabilities and Fund Balances	<u>\$ 163,853</u>	<u>\$ 190,342</u>	<u>\$ 3,371</u>	<u>\$ 3,695</u>

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

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
 Combined Statement of Revenues, Expenditures, and Changes in Fund Balances
~~Fiscal Years Ended September 30~~
 (in thousands)

	Governmental Fund Types	
	Special Revenue	
	1999	1998
REVENUES		
Taxes	\$ 58,524	\$ 57,454
Interest and other miscellaneous	<u>25,850</u>	<u>22,101</u>
Total Revenues	<u>\$ 84,374</u>	<u>\$ 79,555</u>
EXPENDITURES		
Current:		
General government	\$ 780	\$ 898
Environment	<u>63,271</u>	<u>59,664</u>
Total Expenditures	<u>\$ 64,051</u>	<u>\$ 60,562</u>
Excess of Revenues Over (Under) Expenditures	<u>\$ 20,323</u>	<u>\$ 18,993</u>
OTHER FINANCING SOURCES (USES)		
Proceeds from bond issues	\$	\$ 91,198
Operating transfers from other funds	12,003	5,134
Operating transfers to other funds	<u>(40,878)</u>	<u>(35,367)</u>
Total Other Financing Sources (Uses)	<u>\$ (28,875)</u>	<u>\$ 60,965</u>
Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses	\$ (8,552)	\$ 79,958
Fund Balances - Beginning of fiscal year	123,700	10,524
Equity transfers from other funds (Note 4)		<u>33,218</u>
Fund Balances - End of fiscal year	<u>\$ 115,149</u>	<u>\$ 123,700</u>

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

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
 Schedule of General Fund Revenues and Operating Transfers
~~Fiscal Years Ended September 30~~
 (in thousands)

	1999	1998
REVENUES		
Taxes	\$ 829	\$ 858
From federal agencies	32,915	29,687
From local agencies	53	85
From licenses and permits	21,464	19,300
Miscellaneous	20,125	20,416
Total Revenue	\$ 75,386	\$ 70,346
 OPERATING TRANSFERS		
From Michigan Transportation Fund	\$ 780	\$ 692
From Combined Environmental Protection Bond Fund	15,000	
From Michigan Underground Storage Tank Financial Assurance Fund		75
Total Operating Transfers	\$ 15,780	\$ 767
Total Revenues and Operating Transfers	\$ 91,166	\$ 71,113

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

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
Schedule of Sources and Disposition of General Fund Authorizations
Fiscal Years Ended September 30
(in thousands)

	<u>1999</u>	<u>1998</u>
SOURCES OF AUTHORIZATIONS		
General purpose appropriations	\$ 75,148	\$ 34,502
Balances carried forward	65,634	84,835
Restricted financing sources	88,050	68,130
Less: Intrafund expenditure reimbursements	<u>(1,087)</u>	<u>(939)</u>
Total	<u>\$ 227,744</u>	<u>\$ 186,527</u>
 DISPOSITION OF AUTHORIZATIONS		
Gross expenditures and operating transfers out	\$ 138,195	\$ 121,762
Less: Intrafund expenditure reimbursements	<u>(1,087)</u>	<u>(939)</u>
Net expenditures and operating transfers out	<u>\$ 137,108</u>	<u>\$ 120,823</u>
Balances carried forward:		
Multi-year projects	\$ 31,792	\$ 22,008
Encumbrances	6,723	4,574
Restricted revenue (Note 6)	47,048	39,052
Revolving loan programs	<u>5,000</u>	<u></u>
Total balances carried forward	<u>\$ 87,563</u>	<u>\$ 65,634</u>
Balances lapsed	<u>\$ 72</u>	<u>\$ 70</u>
Total	<u>\$ 227,744</u>	<u>\$ 186,527</u>

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

Notes to the Financial Statements and Schedules

Note 1 Significant Accounting Policies

a. Reporting Entity - Financial Statements

The accompanying financial statements report the financial position and results of operations of the following funds as of and for the fiscal years ended September 30, 1999 and September 30, 1998.

The Department of Environmental Quality (DEQ) administers the following funds:

Special Revenue

Combined Environmental Protection Bond Fund (includes Environmental Protection Bond Fund and Clean Michigan Initiative)

Michigan Underground Storage Tank Financial Assurance Fund

Bottle Deposits Fund

Agency

Environmental Quality Deposits Fund

These funds are a part of the State of Michigan entity and are reported on in the *State of Michigan Comprehensive Annual Financial Report (SOMCAFR)*.

b. Reporting Entity - Financial Schedules

The accompanying financial schedules report the results of the governmental operations of DEQ for the fiscal years ended September 30, 1999 and September 30, 1998. The governmental operations of DEQ are accounted for principally in the State's General Fund and are reported on in the *SOMCAFR*. Other DEQ activities related to environmental clean-up are reported in various special revenue funds.

c. Basis of Accounting

The financial statements and schedules contained in this report are prepared on the modified accrual basis of accounting. The modified accrual basis of accounting, which emphasizes the measurement of current financial resource flows, is explained in more detail in the *SOMCAFR*.

d. Basis of Presentation

The accompanying financial statements present only the funds listed in Note 1a. The accompanying financial schedules include only the revenues and operating transfers and the sources and disposition of authorizations for DEQ's General Fund accounts. The *SOMCAFR* provides more extensive general disclosures regarding the State's Summary of Significant Accounting Policies, Budgeting and Budgetary Control, Treasurer's Common Cash, Pension Benefits and Other Postemployment Benefits, Compensated Absences, and Interfund Receivables and Payables.

Accordingly, these financial statements and schedules are not intended to present fairly the financial position and results of operations or to constitute a complete financial presentation of DEQ, the State of Michigan, the State's General Fund, or the State's special revenue and agency funds in accordance with generally accepted accounting principles.

The financial transactions of DEQ are recorded in the General Fund and individual funds in the State's central accounting system. The various environmental quality funds are combined in the *SOMCAFR* into fund types described as follows:

Governmental Fund Types

Special Revenue Funds: This fund group includes operating fund activities financed by specific revenue sources that are legally restricted for specified purposes.

Fiduciary Fund Types

Agency Funds: This group includes assets held by DEQ on behalf of outside parties. DEQ's responsibility is custodial in nature, and the asset and liability balances, but not operating results, are included within these statements.

Note 2 Joint Venture

The State, represented by DEQ, is a participant in a joint venture known as the Great Lakes Protection Fund. The joint venture is not reflected within this report because it did not meet generally accepted accounting principles' criteria for inclusion. A description of the joint venture follows. Complete financial statements may be obtained directly by contacting the Financial Reporting Section, Office of Financial Management, Department of Management and Budget, at (517) 373-3029.

The Great Lakes Protection Fund is a not-for-profit corporation located in Chicago, Illinois. Its purpose is to finance and support research with respect to water quality of the Great Lakes. The eight states bordering on the Great Lakes are eligible to become members if they make a required contribution to the endowment of the Fund. Contribution requirements were established based upon water consumption and usage. Michigan is the largest contributor to the Fund, having made a contribution of \$25 million, constituting approximately 31% of the total. Michigan made its required contribution in fiscal year 1989-90 by issuing the Fund a general obligation bond authorized as part of the State's environmental protection bond program. No additional contributions from Michigan will be required.

Each of the participating seven member states is represented by two members on the Fund's Board of Directors. The Board members are selected by the states' respective governors. The Fund's financing and budgeting operations are controlled by the directors within requirements established by the Articles of Incorporation. Net earnings after operating expenses are divided into parts. One third of the net earnings on total contributions is granted to the respective states in proportion to their contributions to the Fund, to be used for the purposes of the Fund. Two thirds of the net earnings are available to the Fund

to make other grants. The State's equity interest in the Great Lakes Protection Fund of \$25 million is reflected in the *SOMCAFR* in the general fixed assets account group.

Note 3 MUSTFA Obligations

The special revenue fund named the Michigan Underground Storage Tank Financial Assurance (MUSTFA) Fund that is included in this report is not a full presentation of all activities related to the MUSTFA Program. The MUSTFA Finance Authority was established to provide financing, including short- and long-term debt instruments, for the MUSTFA Fund. The Finance Authority's activities are recorded in another special revenue fund and a debt service fund both named Michigan Underground Storage Tank Financial Assurance Finance Authority. Other MUSTFA Program obligations are recorded in the State's general long-term obligations account group. These additional funds and the account group are a part of the State of Michigan reporting entity and are reported on in the *SOMCAFR*.

Other MUSTFA Program financial activities are reported elsewhere as follows (in millions):

	Fiscal Year	
	1998-99	1997-98
Obligations:		
General long-term obligations account group:		
Bonds outstanding	\$ 180.5	\$ 193.6
Claims outstanding	6.2	8.5
Special revenue fund:		
MUSTFA Finance Authority		5.0
Debt service fund:		
MUSTFA Finance Authority	(26.2)	(38.7)
	<hr/>	<hr/>
Net Obligations	<u>\$ 160.5</u>	<u>\$ 168.4</u>

Also see Note 5 and Note 8.

Note 4 Equity Transfers

Equity transfers totaling \$17.4 and \$17.3 million were made from the General Fund in fiscal years 1998-99 and 1997-98, respectively, to provide for State matching of federal funds and revolving fund loan capital for the State Revolving Fund Program within the Michigan Municipal Bond Authority (a discretely presented component unit).

An equity transfer of \$33.2 million was made from the General Fund to the Bottle Deposits Fund in fiscal year 1997-98 to fund the State Site Cleanup Program and for capitalization of the Bottle Deposits Fund.

Note 5 Fund Balance Deficits

The MUSTFA Fund (a special revenue fund) had an unreserved fund deficit of \$37.7 million at September 30, 1999. The deficit was caused by appropriations and payment of claims that exceeded revenue to date.

Note 6 Restricted Revenue

This revenue is restricted, by statute, for use to a particular department program or activity. However, the expenditure of the restricted revenue is subject to annual legislative appropriation.

Note 7 Funds Held as Permanent Investments

Funds held as permanent investments represent amounts that have been legally restricted for the purpose of providing a long-term source of investment income. These investments can include either specific investments held for the fund or portions of the fund's share of the Common Cash pool.

Note 8 Contingencies

The MUSTFA Fund, a special revenue fund, receives revenues dedicated to reimbursing owners/operators of underground storage tanks for costs incurred related to conducting corrective actions at sites where a release has occurred from an underground storage tank. The MUSTFA Fund was declared insolvent and received no additional claims after June 29, 1995. The revenue is still collected to pay off two main obligations of the MUSTFA Fund: the long-term liability for incurred claims recorded in the general long-term obligations account group and the debt and the debt service charges associated with the

financial borrowing mechanisms utilized to expedite reimbursement to eligible owners/operators, which is discussed in Note 3.

Note 9 Subsequent Events

General Long-Term Obligations: In October 1999, \$81.4 million in general obligation bonds were issued under the Clean Michigan Initiative for environmental programs.

On August 24, 2000, DEQ made an arbitrage liability payment of \$709,614 on the 1995 environmental bond issue.

SUPPLEMENTAL FINANCIAL
STATEMENTS AND SCHEDULES

DEPARTMENT OF ENVIRONMENTAL QUALITY
Combining Balance Sheet
Special Revenue Funds
As of September 30
(in thousands)

	Combined Environmental Protection Bond Fund		Michigan Underground Storage Tank Financial Assurance Fund		Bottle Deposits Fund		Totals	
	1999	1998	1999	1998	1999	1998	1999	1998
	ASSETS							
Current Assets:								
Cash	\$	\$	\$	\$	\$ 46	\$ 81	\$ 46	\$ 81
Equity in Common Cash	26,432	80,261	6,380	3,292	106,694	95,801	139,506	179,354
Taxes, interest, and penalties receivable			4,855	5,107			4,855	5,107
Amounts due from other funds	15,248			1,055			15,248	1,055
Amounts due from local units	30						30	
Other current assets	118	116	3	33	1,306	2,424	1,427	2,573
Total Current Assets	\$ 41,828	\$ 80,377	\$ 11,238	\$ 9,487	\$ 108,046	\$ 98,306	\$ 161,112	\$ 188,170
Amounts due from local units					1,330		1,330	
Other noncurrent assets	59	218			1,352	1,954	1,411	2,172
Total Assets	\$ 41,887	\$ 80,595	\$ 11,238	\$ 9,487	\$ 110,727	\$ 100,259	\$ 163,853	\$ 190,342
LIABILITIES AND FUND BALANCES								
Current Liabilities:								
Warrants outstanding	\$ 2,070	\$ 954	\$ 7	\$ 270	\$ 222	\$ 20	\$ 2,299	\$ 1,244
Accounts payable and other liabilities	15,340	13,684	349	320	10,805	9,419	26,494	23,423
Amounts due to other funds	15,248	3	2,862	39,541	16	6	18,126	39,550
Deferred revenue					433	472	433	472
Total Current Liabilities	\$ 32,658	\$ 14,640	\$ 3,219	\$ 40,132	\$ 11,476	\$ 9,916	\$ 47,352	\$ 64,689
Deferred revenue					1,352	1,954	1,352	1,954
Total Liabilities	\$ 32,658	\$ 14,640	\$ 3,219	\$ 40,132	\$ 12,828	\$ 11,870	\$ 48,704	\$ 66,643
Fund Balances:								
Reserves for:								
Budgetary carry-forwards:								
Encumbrances	\$	\$	\$ 1	\$ 5	\$ 4,225	\$	\$ 4,226	\$ 5
Restricted revenues			3,157	2,918	67,896	55,912	71,053	58,830
Multi-year projects			42,608	75,278	18,878		61,486	75,278
Revolving loan programs					2,670		2,670	
Funds held as permanent investments					2,900	1,775	2,900	1,775
Noncurrent assets	59				1,330		1,389	
Total Reserved	\$ 59	\$ 0	\$ 45,766	\$ 78,201	\$ 97,899	\$ 57,687	\$ 143,724	\$ 135,888
Unreserved	9,170	65,955	(37,747)	(108,845)		30,703	(28,575)	(12,189)
Total Fund Balances	\$ 9,229	\$ 65,955	\$ 8,019	\$ (30,644)	\$ 97,899	\$ 88,390	\$ 115,149	\$ 123,700
Total Liabilities and Fund Balances	\$ 41,887	\$ 80,595	\$ 11,238	\$ 9,487	\$ 110,727	\$ 100,259	\$ 163,853	\$ 190,342

DEPARTMENT OF ENVIRONMENTAL QUALITY
Combining Statement of Revenues, Expenditures, and Changes in Fund Balances
Special Revenue Funds
Fiscal Years Ended September 30
(in thousands)

	Combined Environmental Protection Bond Fund		Michigan Underground Storage Tank Financial Assurance Fund		Bottle Deposits Fund		Totals	
	1999	1998	1999	1998	1999	1998	1999	1998
REVENUES								
Taxes	\$	\$	\$ 58,524	\$ 57,454	\$	\$	\$ 58,524	\$ 57,454
Interest and other miscellaneous	3,850	1,920	73	487	21,927	19,694	25,850	22,101
Total Revenues	<u>\$ 3,850</u>	<u>\$ 1,920</u>	<u>\$ 58,596</u>	<u>\$ 57,940</u>	<u>\$ 21,927</u>	<u>\$ 19,694</u>	<u>\$ 84,374</u>	<u>\$ 79,555</u>
EXPENDITURES								
Current:								
General government	\$	\$	\$ 780	\$ 898	\$	\$	\$ 780	\$ 898
Environment	37,567	33,658	5,458	6,991	20,246	19,015	63,271	59,664
Total Expenditures	<u>\$ 37,567</u>	<u>\$ 33,658</u>	<u>\$ 6,237</u>	<u>\$ 7,888</u>	<u>\$ 20,246</u>	<u>\$ 19,015</u>	<u>\$ 64,051</u>	<u>\$ 60,562</u>
Excess of Revenues Over (Under) Expenditures	<u>\$ (33,718)</u>	<u>\$ (31,738)</u>	<u>\$ 52,359</u>	<u>\$ 50,052</u>	<u>\$ 1,681</u>	<u>\$ 679</u>	<u>\$ 20,323</u>	<u>\$ 18,993</u>
OTHER FINANCING SOURCES (USES)								
Proceeds from bond issues	\$	\$ 91,198	\$	\$	\$	\$	\$	\$ 91,198
Operating transfers from other funds			4,000	4,000	8,003	1,134	12,003	5,134
Operating transfers to other funds	(23,008)	(1,149)	(17,696)	(34,122)	(174)	(96)	(40,878)	(35,367)
Total Other Financing Sources (Uses)	<u>\$ (23,008)</u>	<u>\$ 90,049</u>	<u>\$ (13,696)</u>	<u>\$ (30,122)</u>	<u>\$ 7,829</u>	<u>\$ 1,037</u>	<u>\$ (28,875)</u>	<u>\$ 60,965</u>
Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses	<u>\$ (56,726)</u>	<u>\$ 58,311</u>	<u>\$ 38,663</u>	<u>\$ 19,930</u>	<u>\$ 9,510</u>	<u>\$ 1,716</u>	<u>\$ (8,552)</u>	<u>\$ 79,958</u>
Fund Balances - Beginning of fiscal year	65,955	7,644	(30,644)	(50,575)	88,390	53,455	123,700	10,524
Equity transfers from other funds						33,218		33,218
Fund Balances - End of fiscal year	<u>\$ 9,229</u>	<u>\$ 65,955</u>	<u>\$ 8,019</u>	<u>\$ (30,644)</u>	<u>\$ 97,899</u>	<u>\$ 88,390</u>	<u>\$ 115,149</u>	<u>\$ 123,700</u>

DEPARTMENT OF ENVIRONMENTAL QUALITY
 Balance Sheet
 Combined Environmental Protection Bond Fund
 Fiscal Years Ended September 30
 (in thousands)

	Environmental Protection Bond Fund		Clean Michigan Initiative Bond Fund	
	1999	1998	1999	1998
ASSETS				
Equity in Common Cash	\$ 26,432	\$ 80,261	\$	\$
Amounts due from other funds	15,248			
Amounts due from local units	30			
Other current assets	118	116		
Total Current Assets	\$ 41,828	\$ 80,377	\$ 0	\$ 0
Other noncurrent assets	59	218		
Total Assets	\$ 41,887	\$ 80,595	\$ 0	\$ 0
LIABILITIES AND FUND BALANCES				
Liabilities:				
Warrants outstanding	\$ 2,069	\$ 954	\$ 1	\$
Accounts payable and other liabilities	14,630	13,684	710	
Amounts due to other funds		3	15,248	
Total Current Liabilities	\$ 16,699	\$ 14,640	\$ 15,959	\$ 0
Total Liabilities	\$ 16,699	\$ 14,640	\$ 15,959	\$ 0
Fund Balances:				
Reserves for:				
Noncurrent assets	\$ 59	\$	\$	\$
Total Reserved	\$ 59	\$ 0	\$ 0	\$ 0
Unreserved	25,129	65,955	(15,959)	
Total Fund Balances	\$ 25,188	\$ 65,955	\$ (15,959)	\$ 0
Total Liabilities and Fund Balances	\$ 41,887	\$ 80,595	\$ 0	\$ 0

<u>Totals</u>	
<u>1999</u>	<u>1998</u>
\$ 26,432	\$ 80,261
15,248	
30	
<u>118</u>	<u>116</u>
\$ 41,828	\$ 80,377
<u>59</u>	<u>218</u>
<u>\$ 41,887</u>	<u>\$ 80,595</u>
\$ 2,070	\$ 954
15,340	13,684
<u>15,248</u>	<u>3</u>
\$ 32,658	\$ 14,640
<u>\$ 32,658</u>	<u>\$ 14,640</u>
\$ 59	\$
\$ 59	\$ 0
<u>9,170</u>	<u>65,955</u>
\$ 9,229	\$ 65,955
<u>\$ 41,887</u>	<u>\$ 80,595</u>

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
Statement of Revenues, Expenditures, and Changes in Fund Balances
Combined Environmental Protection Bond Fund
~~Fiscal Years Ended September 30~~
(in thousands)

	<u>Environmental Protection Bond Fund</u>		<u>Clean Michigan Initiative Bond Fund</u>	
	<u>1999</u>	<u>1998</u>	<u>1999</u>	<u>1998</u>
REVENUES				
Interest and other miscellaneous	\$ 3,850	\$ 1,920	\$	\$
Total Revenues	<u>\$ 3,850</u>	<u>\$ 1,920</u>	<u>\$ 0</u>	<u>\$ 0</u>
EXPENDITURES				
Current:				
Environmental	<u>\$ 36,608</u>	<u>\$ 33,658</u>	<u>\$ 959</u>	<u>\$</u>
Total Expenditures	<u>\$ 36,608</u>	<u>\$ 33,658</u>	<u>\$ 959</u>	<u>\$ 0</u>
Excess of Revenues Over (Under) Expenditures	<u>\$ (32,759)</u>	<u>\$ (31,738)</u>	<u>\$ (959)</u>	<u>\$ 0</u>
OTHER FINANCING SOURCES (USES)				
Proceeds from bond issues	\$	\$ 91,198	\$	\$
Operating transfers to other funds	<u>(8,008)</u>	<u>(1,149)</u>	<u>(15,000)</u>	<u></u>
Total Other Financing Sources (Uses)	<u>\$ (8,008)</u>	<u>\$ 90,049</u>	<u>\$ (15,000)</u>	<u>\$ 0</u>
Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses	\$ (40,767)	\$ 58,311	\$ (15,959)	\$
Fund Balances - Beginning of fiscal year	65,955	7,644		
Fund Balances - End of fiscal year	<u>\$ 25,188</u>	<u>\$ 65,955</u>	<u>\$ (15,959)</u>	<u>\$ 0</u>

<u>Totals</u>	
<u>1999</u>	<u>1998</u>
<u>\$ 3.850</u>	<u>\$ 1.920</u>
<u>\$ 3.850</u>	<u>\$ 1.920</u>
<u>\$ 37.567</u>	<u>\$ 33.658</u>
<u>\$ 37.567</u>	<u>\$ 33.658</u>
<u>\$ (33,718)</u>	<u>\$ (31,738)</u>
\$	\$ 91,198
<u>(23,008)</u>	<u>(1,149)</u>
<u>\$ (23,008)</u>	<u>\$ 90,049</u>
\$ (56,726)	\$ 58,311
65,955	7,644
<u>\$ 9,229</u>	<u>\$ 65,955</u>

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
 Statement of Changes in Assets and Liabilities
 Environmental Quality Deposits Fund
~~Fiscal Years Ended September 30, 1999~~
 (in thousands)

	<u>Balance</u> October 1, 1998	<u>Additions</u>	<u>Deductions</u>	<u>Balance</u> September 30, 1999
ASSETS				
Current Assets:				
Equity in Common Cash	\$ 3,695	\$ 1,024	\$ 1,348	\$ 3,371
Total Assets	<u>\$ 3,695</u>	<u>\$ 1,024</u>	<u>\$ 1,348</u>	<u>\$ 3,371</u>
 LIABILITIES				
Current Liabilities:				
Accounts payable and other liabilities	\$ 3,695	\$ 1,024	\$ 1,348	\$ 3,371
Total Liabilities	<u>\$ 3,695</u>	<u>\$ 1,024</u>	<u>\$ 1,348</u>	<u>\$ 3,371</u>

~~DEPARTMENT OF ENVIRONMENTAL QUALITY~~
 Statement of Changes in Assets and Liabilities
 Environmental Quality Deposits Fund
~~Fiscal Years Ended September 30, 1998~~
 (in thousands)

	Balance October 1, 1997	Additions	Deductions	Balance September 30, 1998
ASSETS				
Current Assets:				
Cash	\$ 4	\$	\$ 4	\$
Equity in Common Cash	3,415	325	45	3,695
Total Assets	\$ 3,419	\$ 325	\$ 49	\$ 3,695
LIABILITIES				
Current Liabilities:				
Accounts payable and other liabilities	\$ 3,419	\$ 321	\$ 45	\$ 3,695
Total Liabilities	\$ 3,419	\$ 321	\$ 45	\$ 3,695

DEPARTMENT OF ENVIRONMENTAL QUALITY
Schedule of Expenditures of Federal Awards (1)
For the Period October 1, 1997 through September 30, 1999

For the Fiscal Year Ended September 30, 1998

Federal Agency/Program	CFDA (2) Number	Pass-Through Identification Number	Transferred to Other State Agencies	Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
U.S. Department of Commerce						
Direct Program						
Coastal Zone Management Administration Awards	11.419		\$ 114,698	\$ 1,538,614	\$ 837,356	\$ 2,490,668
Total U.S. Department of Commerce			\$ 114,698	\$ 1,538,614	\$ 837,356	\$ 2,490,668
U.S. Department of Defense						
Direct Program						
State Memorandum of Agreement Program for the Reimbursement of Technical Services	12.113		\$	\$ 496,748	\$	\$ 496,748
Total U.S. Department of Defense			\$ 0	\$ 496,748	\$ 0	\$ 496,748
U.S. Department of the Interior						
Direct Programs						
U.S. Fish and Wildlife Service	15.000		\$	\$ 4,992	\$	\$ 4,992
Wildlife Conservation and Appreciation	15.617					
U.S. Geological Survey - Research and Data Acquisition	15.808			29,438	40,814	70,252
National Cooperative Geologic Mapping Program	15.810					
State Partnerships	15.977				10,165	10,165
Total U.S. Department of the Interior			\$ 0	\$ 34,431	\$ 50,979	\$ 85,410
U.S. Environmental Protection Agency						
Direct Programs						
Air Pollution Control Program Support	66.001		\$	\$ 2,314,494	\$	\$ 2,314,494
State Indoor Radon Grants	66.032			188,225	72,991	261,216
Water Pollution Control - State and Interstate Program Support	66.419			2,772,634		2,772,634
State Public Water System Supervision	66.432		41,435	4,321,845		4,363,280
Water Pollution Control - Lake Restoration Cooperative Agreements	66.435			2,530	29,807	32,337
Water Quality Management Planning	66.454			346,631	235,261	581,892
Capitalization Grants for State Revolving Funds	66.458		126,064	1,822,775	89,023,023	90,971,862
Nonpoint Source Implementation Grants	66.460		78,744	846,905	2,039,850	2,965,499
Wetlands Protection - Development Grants	66.461		2,166	139,428	247,985	389,579
National Pollutant Discharge Elimination System Related State Program Grants	66.463			249,344	51,670	301,014
Wastewater Operator Training Grant Program	66.467					
Capitalization Grants for Drinking Water State Revolving Funds	66.468			1,042,517	1,573,793	2,616,310
Great Lakes Program	66.469			185,715		185,715
Water Pollution Control - Research, Development, and Demonstration	66.505			9,112	10,000	19,112
Surveys, Studies, Investigations, and Special Purpose Grants	66.606		20,000	815,205		835,205
Training and Fellowships for the Environmental Protection Agency	66.607			73,005		73,005
Pollution Prevention Grants Program	66.708			64,957		64,957
Hazardous Waste Management State Program Support	66.801		32,000	3,130,627		3,162,628
Superfund State Site - Specific Cooperative Agreements	66.802			1,872,046		1,872,046
State Underground Storage Tanks Program	66.804			209,700		209,700

This schedule continued on next page.

For the Fiscal Year Ended September 30, 1999				
Transferred to Other State Agencies	Directly Expended	Distributed to Subrecipients	Total Expended and Distributed	Total Expended and Distributed for the Two-Year Period
\$ 70,136	\$ 1,553,082	\$ 878,899	\$ 2,502,117	\$ 4,992,784
\$ 70,136	\$ 1,553,082	\$ 878,899	\$ 2,502,117	\$ 4,992,784
\$	\$ 392,316	\$	\$ 392,316	\$ 889,063
\$ 0	\$ 392,316	\$ 0	\$ 392,316	\$ 889,063
\$	\$ 2,523	\$	\$ 2,523	\$ 4,992
		23,594	23,594	2,523
		85,023	85,023	93,846
				85,023
				10,165
\$ 0	\$ 2,523	\$ 108,617	\$ 111,140	\$ 196,550
\$	\$ 2,232,553	\$	\$ 2,232,553	\$ 4,547,047
	178,438	94,825	273,263	534,479
22,647	4,057,106	27,557	4,107,309	6,879,943
	3,957,660		3,957,660	8,320,941
	22,947		22,947	55,284
	151,710	180,371	332,081	913,972
164,442	1,709,418	73,571,800	75,445,660	166,417,522
75,000	735,450	2,084,950	2,895,401	5,860,899
	216,243	192,596	408,839	798,418
	194,497	91,089	285,586	586,599
	45,295		45,295	45,295
	1,915,058	31,427,314	33,342,372	35,958,682
	79,788	123,205	202,993	388,708
				19,112
20,000	929,242	134,364	1,083,606	1,918,811
	6,616		6,616	79,621
	60,896		60,896	125,854
43,647	3,211,395	9,571	3,264,614	6,427,242
	2,434,678	1,238,000	3,672,678	5,544,724
	186,000		186,000	395,700

DEPARTMENT OF ENVIRONMENTAL QUALITY
Schedule of Expenditures of Federal Awards (1)
For the Period October 1, 1997 through September 30, 1999
Continued

For the Fiscal Year Ended September 30, 1998						
Federal Agency/Program	CFDA (2) Number	Pass-Through Identification Number	Transferred to Other State Agencies	Directly Expended	Distributed to Subrecipients	Total Expended and Distributed
Leaking Underground Storage Tank Trust Fund Program	66.805		\$ 11,110	\$ 1,881,310		\$ 1,892,420
Solid Waste Management Assistance	66.808			8,689		8,689
Superfund State Core Program Cooperative Agreements	66.809		616	1,000,355		1,000,971
Total Direct Programs			<u>\$ 312,135</u>	<u>\$ 23,298,047</u>	<u>\$ 93,284,381</u>	<u>\$ 116,894,563</u>
Pass-Through Programs						
Wayne County						
Great Lakes Program	66.469	A995353-02	\$	\$	\$	\$
Great Lakes Commission						
Surveys, Studies, Investigations, and Special Purpose Grants	66.606	X995743-02		248,439		248,439
Total Pass-Through Programs			<u>\$ 0</u>	<u>\$ 248,439</u>	<u>\$ 0</u>	<u>\$ 248,439</u>
Total U.S. Environmental Protection Agency			<u>\$ 312,135</u>	<u>\$ 23,546,486</u>	<u>\$ 93,284,381</u>	<u>\$ 117,143,002</u>
Nuclear Regulatory Commission						
Direct Program						
Radiation Control - Training Assistance and Advisory Counseling	77.001		\$	7,500	\$	7,500
Total Nuclear Regulatory Commission			<u>\$ 0</u>	<u>\$ 7,500</u>	<u>\$ 0</u>	<u>\$ 7,500</u>
Federal Emergency Management Agency						
Direct Program						
Hazard Mitigation Grant	83.548		\$	15,419	\$	15,419
Pass-Through Programs						
Michigan Department of State Police						
Community Assistance Program - State Support Services Element	83.105	EMC-98-PA-1337	\$	164,021	\$	164,021
Community Assistance Program - State Support Services Element	83.105	EMC-99-PA-1343				0
Flood Mitigation Assistance	83.536	EMC-00-PA-1337				0
Total Pass-Through Programs			<u>\$ 0</u>	<u>\$ 164,021</u>	<u>\$ 0</u>	<u>\$ 164,021</u>
Total Federal Emergency Management Agency			<u>\$ 0</u>	<u>\$ 179,440</u>	<u>\$ 0</u>	<u>\$ 179,440</u>
Total Expenditures of Federal Awards			<u>\$ 426,833</u>	<u>\$ 25,803,218</u>	<u>\$ 94,172,716</u>	<u>\$ 120,402,767</u>

(1) Basis of Presentation: This schedule includes the federal grant activity of the Department of Environmental Quality and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements and schedules.

(2) CFDA is defined as *Catalog of Federal Domestic Assistance*.

<u>For the Fiscal Year Ended September 30, 1999</u>				
<u>Transferred to Other State Agencies</u>	<u>Directly Expended</u>	<u>Distributed to Subrecipients</u>	<u>Total Expended and Distributed</u>	<u>Total Expended and Distributed for the Two-Year Period</u>
\$ 25,403	\$ 1,228,553	\$	\$ 1,253,956	\$ 3,146,376
	1,133,974		1,133,974	8,689
<u>\$ 351,139</u>	<u>\$ 24,687,517</u>	<u>\$ 109,175,643</u>	<u>\$ 134,214,299</u>	<u>\$ 251,108,863</u>
\$	\$ 79,111	\$	\$ 79,111	\$ 79,111
	47,646		47,646	296,085
<u>\$ 0</u>	<u>\$ 126,757</u>	<u>\$ 0</u>	<u>\$ 126,757</u>	<u>\$ 375,196</u>
<u>\$ 351,139</u>	<u>\$ 24,814,275</u>	<u>\$ 109,175,643</u>	<u>\$ 134,341,057</u>	<u>\$ 251,484,059</u>
<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$ 0</u>	<u>\$ 7,500</u>
<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 7,500</u>
<u>\$ 0</u>	<u>\$ 1,655</u>	<u>\$ 0</u>	<u>\$ 1,655</u>	<u>\$ 17,074</u>
\$	\$	\$	\$ 0	\$ 164,021
	170,817		170,817	170,817
	12,023		12,023	12,023
<u>\$ 0</u>	<u>\$ 182,840</u>	<u>\$ 0</u>	<u>\$ 182,840</u>	<u>\$ 346,861</u>
<u>\$ 0</u>	<u>\$ 184,495</u>	<u>\$ 0</u>	<u>\$ 184,495</u>	<u>\$ 363,935</u>
<u>\$ 421,275</u>	<u>\$ 26,946,691</u>	<u>\$ 110,163,160</u>	<u>\$ 137,531,125</u>	<u>\$ 257,933,890</u>

OTHER SCHEDULES

DEPARTMENT OF ENVIRONMENTAL QUALITY

Summary Schedule of Prior Audit Findings
As of September 30, 1999

PRIOR AUDIT FINDINGS RELATED TO THE FINANCIAL STATEMENTS AND SCHEDULES

Audit Findings That Have Been Fully Corrected:

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 1

Finding: The Drinking Water and Radiological Protection Division (DWRPD) did not separate its cash receipting and accounts receivable recording functions or have a system of controls to compensate for the lack of separation of duties within DWRPD.

Comments: The Department of Environmental Quality (DEQ) agrees with this finding and has taken steps to separate its cash receipting and accounts receivable recording functions in DWRPD. By June 30, 1999, the necessary data system modifications were completed. Also in June 1999, the following steps were taken to separate duties and improve internal control over cash receipting and accounts receivable recording. Cash received in the laboratory for prepaid water testing is restrictively endorsed, posted to the internal accounts receivable system, receipted via preparation of a cash log (two employees involved, both running a tape), and transmitted directly to DEQ Revenue Control. All cash received in DWRPD's Administration Section from a mailed invoice is opened by the Section secretary. Checks are restrictively endorsed and checks and cash are posted to the accounts receivable system by two data coding operators. Both data coding operators are involved in the preparation of the cash log, each running a separate tape. Cash and checks are then transmitted to DEQ Revenue Control. Invoices for water tested are generated in the data processing area and reviewed by both data coding operators before mailing. DWRPD has implemented a procedure to reconcile its cash log transmittals to DEQ Revenue Control with revenue deposits in the

Michigan Administrative Information Network (MAIN). This reconciliation is performed monthly. DWRPD will continue its efforts to develop and implement a method to reconcile its internal accounts receivable system with the cash receipts recorded in MAIN.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 2

Finding: DEQ did not prepare daily control logs of transactions entered into the Personnel-Payroll Information System for Michigan (PPRISM).

Comments: DEQ agrees that, at the time the audit was performed, the control log was not generated or transactions reconciled to it. As of August 1998, the Office of Personnel Services implemented a process where the supervisor of the Office generates the daily control logs and reconciles the number of transactions to the log.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 3

Finding: DEQ did not separate PPRISM duties between the transaction operators and the agency master operator.

Comments: DEQ agrees that transaction operators have been given access to the PPRISM PSWU code (a transaction code to change, delete, and update passwords for PPRISM users). However, they only use it to give passwords to those operators already established in the system. Only the DEQ master operator establishes new users and inactivates them in the system. Even though the transaction operators have the ability to establish or change operator capabilities, DEQ uses compensating controls to monitor activity. The CNTL code was implemented in August 1998 and is now used daily to review the instances of PSWU code use, and the State of Michigan PPRISM valid operators report (CR-185) is monitored to review current users and their status.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 10

Finding: DEQ and the Department of Management and Budget (DMB) did not transfer fiscal year 1996-97 unclaimed bottle deposit revenue spending authorization from the General Fund to the Bottle Deposits Fund.

Comments: DEQ agrees and has complied. DMB transferred the spending authority for the Bottle Deposits Fund from the General Fund. The entry was processed in MAIN on November 24, 1998.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 11

Finding: The Environmental Response Division had not developed a method for estimating fiscal year-end accounts payable, resulting in misstatements of expenditures and accounts payable in the Environmental Protection Bond Fund and the General Fund.

Comments: DEQ partially agrees. Work on these sites spans fiscal years and experience shows that it is difficult to obtain estimates from vendors in order to establish accounts payable. Additionally, these appropriations have work project authorization. Given the multi-year nature of contaminated site remediation, the contracts are encumbered when issued. In addition, past efforts to estimate accounts payable resulted in criticism regarding the amount of adjustments and write-offs that were required. For fiscal year 1998-99, additional efforts have been made to address the accounts payable issue. Year-end letters were sent to impacted vendors requesting invoice submission or estimated invoice submission. Two follow-up reminder letters were sent prior to the requested deadline for submission. These letters resulted in many vendors submitting estimated invoices. The accuracy of the estimates cannot be determined at this time; therefore, the number of adjustments and write-offs is unknown. Vendors holding contracts with terms requiring submissions of year-end expenses or estimates within specific time frames were notified that this contract language would be enforced. Noncompliance would result in complaint to vendor paperwork being filed. All impacted vendors complied in full. It is the intent to have all contracts contain language regarding submission of year-end expenses or estimates

within specific time frames. DEQ anticipates that this will be addressed in fiscal year 1999-2000.

PRIOR AUDIT FINDINGS RELATED TO FEDERAL AWARDS

Audit Findings That Have Been Fully Corrected:

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 5

Finding: DEQ did not monitor subrecipients in accordance with the Single Audit Act and federal regulations.

- a. DEQ did not receive Single Audit reports from all subrecipients, and many did not meet Single Audit requirements.
- b. DEQ did not always ensure that divisions obtained required performance and financial reports from grant subrecipients.
- c. Although DEQ required State Revolving Fund (SRF) Program subrecipients to submit Single Audit reports to the Division of Local Audit and Finance, DEQ did not verify that the Division had developed a system to review and follow up on submitted reports.

Comments: DEQ agrees with Findings 5a. and 5c. and has taken action in fiscal year 1998-99 to strengthen its subrecipient monitoring program. In addition, DEQ will meet with the Michigan Municipal Bond Authority in December 2000 to clarify the responsibility for review and follow-up of submitted Single Audit reports.

DEQ agrees in part with Finding 5.b. Performance or financial reports are not always received on a timely basis from the grant recipients and a number of reasons exists for this to happen. It could be that either work is not done for a period of time or billings are not received from contractors. Program staff make every effort to obtain information from subrecipients when there is something to report. Beginning in fiscal year 1999-2000, program staff will send quarterly letters with blank performance and financial report forms to all grantees to remind them of their reporting requirements and

deadlines. Furthermore, contract language allows for a 25% holdback until all conditions of the grant are met. Without reports, payments will not be processed. These are DEQ's controls to ensure that reporting requirements are met before payments are made. At fiscal year-end, if the grant period has ended but not all contractual obligations are fulfilled, an account payable is established and maintained until conditions are met. If the project tasks are not completed or required reports are not received, payment is not made for the final 25% and the account payable is written off. In addition, a project audit is conducted and the recipient is required to reimburse the State for any paid but unearned grant funds. If requirements are still not fulfilled when the overall federal grant to DEQ expires, any open contracts are immediately closed.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 6

Finding: DEQ did not properly allocate payroll expenditures to federal grant programs.

- a. Certain staff costs charged to the SRF Program were allocated based on a budget rather than actual time worked or an approved methodology.
- b. Certain Land and Water Management Division administrative staff time sheets did not report the actual time worked on Coastal Zone Management Administration Awards grant activities.
- c. Surface Water Quality Division employees working on the Water Pollution Control - State and Interstate Program Support Grant (CFDA #66.419) maintained biweekly activity logs; however, these logs were not used to bill the federal program.

Comments: DEQ agrees with this finding. Relative to Findings 6.a. and 6.b., as of October 1, 1999, the Environmental Assistance Division and the Land and Water Management Division will begin the implementation of a cost methodology to base the allocation of administrative staff time on the actual hours that nonadministrative staff work on grants. On a quarterly basis, a comparison will be

made of allocated administrative staff time to the actual time worked by nonadministrative staff on various federal awards. Adjustments will be made to the budgeted administrative staff allocations so that the costs recorded reflect actual time worked by nonadministrative staff. With regard to Finding 6.c., nonadministrative staff in the Surface Water Quality Division will begin in March 2000 recording actual time worked on the Section 106 program in the Data Collection and Distribution System (DCDS). This will ensure that the payroll costs recorded in the accounting system will reflect actual hours worked.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 7

Finding: DEQ inappropriately charged terminal leave payments to federal grant programs using a direct cost method without obtaining prior approval of the method from the cognizant federal agency.

Comments: DEQ agrees and has obtained retroactive approval from the U.S. Environmental Protection Agency (EPA) on April 26, 1999 for the use of a direct cost methodology with year-end adjustments. This will necessitate a review of the allocation of these costs for the fiscal years in which these terminal leave payments are charged to the grants. A review of these charges was performed for fiscal years 1996-97, 1997-98, and 1998-99. Charges to the grants were adjusted to ensure that the terminal leave costs charged to the federal programs did not exceed what would have been charged if a special terminal leave rate had been used.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 8

Finding: DEQ did not accurately compute the indirect cost rate for fiscal year 1995-96 and did not maintain documentation of its computation of the indirect cost rate and audit rate for both fiscal years of our audit.

Comments: DEQ agrees. During the first year of the audit period, the accounting staff responsible for preparing the indirect rate remained with the Department of Natural Resources (DNR). This indirect rate

had been negotiated by DNR with its cognizant agency, the U.S. Department of the Interior. In fiscal year 1998-99, when DNR finalized the fiscal year 1995-96 rates, this error was addressed. An adjustment was factored into and finalized as part of the negotiation of the settlement, reached on August 12, 1999, for the fiscal year 1995-96 rates, in accordance with standard procedures to address such errors. After the split of DNR, for the preparation of DEQ's indirect rate for fiscal year 1997-98, DEQ retained the services of the same consulting firm contracted by DMB to prepare the Statewide Cost Allocation Plan. DEQ contracted with this firm on March 19, 1999 to prepare the settlement of fiscal year 1996-97 and the preparation of the indirect rate proposal for fiscal year 1999-2000. This consulting firm has significant experience in developing indirect rates and will ensure the accurate computation and appropriate documentation of the indirect rates.

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 9

Finding: DEQ did not use funds from SRF in accordance with federal regulations.

Comments: DEQ agrees and has complied. The Drinking Water State Revolving Fund's (DWSRF's) enabling legislation was not established in time to obtain an appropriation for fiscal year 1996-97. To comply with the federal guidelines that allowed DEQ to recover expenditures related to the establishment of DWSRF, DEQ recorded these costs in the fiscal year 1996-97 SRF appropriations with coding which indicated that they should be funded with DWSRF money. The expenditures were then reimbursed by DWSRF when the funds were available on July 31, 1998.

Audit Findings Not Corrected or Partially Corrected:

Audit Period: October 1, 1995 through September 30, 1997

Finding Number: 4

Finding: Single Audit reports from subrecipient municipalities did not identify disbursements that the municipalities received from SRF as federal financial assistance.

Comments: DEQ disagrees with this finding. This finding contradicts Finding 5.c., which states that DEQ required SRF Program subrecipients to submit Single Audit reports. Confusion has existed within the State and across the country over the nature of these funds given that the federal grant capitalizes SRF. Despite this confusion, DEQ has held the subrecipients accountable for federal subrecipient requirements, including the Single Audit Act and Minority Business Enterprise/Women Business Enterprise requirements. DEQ does not send a separate letter to municipalities advising them of the audit requirement because the program brochure, the annual intended use plan, and, more importantly, the application that is signed by the municipal applicant identify the federal capitalization grants. Specifically, Part II, Page 8, Section 8 of the loan application references the Single Audit Act requirements. This application is specifically mentioned in the Supplemental Agreement signed by the municipality and the Michigan Municipal Bond Authority at loan closing. Additionally, the most recent EPA review of the SRF Program found that the Program complies with federal statutes and regulations. Despite DEQ's disagreement with this finding, it has taken steps since the audit to further clarify the nature of these funds. DEQ has consulted with the EPA, other states, and a public accounting firm on this issue. Based on this review, it has been determined that because Michigan utilizes a leveraged bond program, federal money does not go directly to loan recipients but rather loans are made from a bond sale. Federal grant funds, when drawn, are placed in a reserve fund. In cases where loans were made prior to 1994 (direct loan), the Single Audit Act applied and DEQ will take appropriate steps to make notification and will follow up to ensure compliance. Also, with regard to the Safe Drinking Water Act, there are specific provisions to provide additional assistance to disadvantaged communities to pay for the planning cost out of the Technical Assistance set aside. In these instances, the funds are considered federal and, when the

assistance is provided, a letter notifying of such and the amount will be sent advising of the U.S. Office of Management and Budget Circular A-133 audit requirement. In addition, the EPA/State work group is evaluating the Single Audit Act issues, and any resulting directives from EPA will result in appropriate response and action to ensure DEQ's compliance with necessary audit issues.

DEPARTMENT OF ENVIRONMENTAL QUALITY

Corrective Action Plan
As of November 14, 2000

FINDINGS RELATED TO THE FINANCIAL STATEMENTS AND SCHEDULES

Finding Number: 760001

Finding Title: Personnel and Payroll Functions

Item: 1.a.

Management Views: **The Department of Environmental Quality (DEQ) agrees in part.**

The Office of Personnel Services did establish and implement internal control for personnel and payroll functions as a result of the previous Single Audit. The transactions staff supervisor at that time followed these procedures. When this person was replaced, the expectation to follow these procedures was not communicated to the new transactions staff supervisor. Therefore, only portions of the monitoring process were being performed.

Corrective Action: When this lack of control was brought to the attention of the Office of Personnel Services, the more thorough review was re-instituted (April 1, 2000). To ensure that this process continues, follow-up will take place quarterly to ensure that the daily transaction control monitoring is being conducted.

Anticipated Completion Date: April 1, 2000

Responsible Individual: Ila Nickerson, Operations Manager, Office of Personnel Services

Item: 1.b.
Management Views: **DEQ agrees in part.**

DEQ agrees that transaction operators have been given access to the PSWU code. They only use it to give passwords to those operators who are already in the system and at a level below their security. Only the DEQ master operator establishes new users or inactivates existing users in the system.

The DEQ master operator uses the Personnel-Payroll Information System for Michigan (PPRISM) valid operators report (CR-185) to monitor new users and to verify deletion of users. This was consistently done throughout the audit period. The daily transaction control log, which was not utilized for a period of time as discussed in item a., provides information about code usage and passwords. From a security perspective, the monitoring of the valid operators report is more critical because that report identifies new users. Although less critical for this function, DEQ has re-instituted use of the daily transaction control log as indicated in item a.

Corrective Action: None
Anticipated Completion Date: April 1, 2000
Responsible Individual: Ila Nickerson, Operations Manager, Office of Personnel Services

Item: 1.c.
Management Views: DEQ agrees.
Corrective Action: The Office of Personnel Services has established the necessary process to monitor PPRISM input by using the daily transaction control log that is completed and reconciled daily against the CNTL transaction in PPRISM (re-instituted April 1, 2000). In addition, a written directive was issued August 16, 2000 to all staff

instructing them on the proper procedure to process transactions that are of a personal effect.

Anticipated Completion Date: April 1, 2000

Responsible Individual: Ila Nickerson, Operations Manager, Office of Personnel Services

Item: 1.d.

Management Views: DEQ disagrees.

The biweekly reconciliation recommended would be redundant with the daily reconciliation discussed in item a. DEQ agrees with conducting the daily reconciliation but does not feel that the redundant biweekly reconciliations are warranted. Existing resources allow for one level of reconciliation to be completed, and DEQ feels that daily reconciliations offer the greatest opportunity to detect and correct errors.

Corrective Action: None

Anticipated Completion Date: Not applicable

Responsible Individual: Ila Nickerson, Operations Manager, Office of Personnel Services

Finding Number: 760002

Finding Title: Accounts Payable Estimation

Management Views: DEQ agrees with this finding. Providing alternate drinking water supplies at sites of groundwater contamination involves contractual arrangements that frequently span more than one fiscal year. It is often difficult for grantees to obtain reasonable estimates from vendors in order to establish accounts payable. Given the multi-year nature of these work projects, the contracts are encumbered when issued and charged to the appropriate appropriation year.

Corrective Action: DEQ will work with grantees to estimate accounts payable where necessary and to separate requests for reimbursement by fiscal year. Despite the best efforts of staff, vendors are occasionally unable to provide reasonable estimates or submit invoices for work prior to the mid-November cut-off for processing payments as old-year expenditures. Any requests for payment of old-year expenditures in the new year must be approved by the Department of Management and Budget, and DEQ ensures that this procedure is followed. Contractual language specifically requires submittal of a financial status report at year-end closing.

Anticipated Completion Date: November 2000

Responsible Individual: Flint Watt, Chief, Drinking Water and Radiological Protection Division

FINDINGS RELATED TO FEDERAL AWARDS

Finding Number: 760003

Finding Title: State Revolving Fund (SRF) Program Subrecipient Designation

Management Views: DEQ disagrees with this finding, as it did for the last Single Audit report.

The audit report states (referring to U.S. Environmental Protection Agency [EPA] Program Guidance): "Also, this guidance states that funds directly [emphasis added] made available to the municipalities from the SRF and DWSRF Capitalization Grants should be considered federal funds subject to the terms of the Single Audit Act." As previously stated, Michigan utilizes a leveraged bond program, in essence purchasing local debt. No federal grant funds go directly to loan recipients, thus the

requirements of U.S. Office of Management and Budget Circular A-133 do not apply.

Michigan will continue to work with other states and the EPA through a task force formed to specifically address this issue.

DEQ will continue to require that loans made prior to 1994 comply with the Single Audit Act. Funds for the Technical Assistance set-aside in the Drinking Water State Revolving Fund for disadvantaged communities will be identified as federal, and communities receiving this assistance will be notified of the Circular A-133 requirements.

Corrective Action: None proposed at this time.
Anticipated Completion Date: Not applicable
Responsible Individual: Paul Zugger, Chief, Environmental Assistance Division
Tom Kamppinen, Chief, Municipal Facilities Section, Environmental Assistance Division

Finding Number: 760004
Finding Title: Federal Grant Payroll Cost Allocation

Item: 4.a.
Management Views: DEQ agrees that the process used to charge payroll costs to the Water Pollution Control grant was not done in accordance with federal requirements during the time period covered by this audit.

Corrective action to address this issue was implemented during fiscal year 1999-2000 in response to the finding in the previous Single Audit. That audit was delayed because of the split of the Department of Natural Resources and the formation of DEQ. Given the time needed to evaluate options and make a decision on the best alternative, fiscal year 1999-2000

was the earliest that corrective action could be implemented.

Corrective Action: Corrective action has already been completed with the implementation of actual activity reporting on the Data Collection and Distribution System (DCDS).

Anticipated Completion Date: Corrective action was completed in March 2000.

Responsible Individual: Ruby Grimes, Chief, Budget and Administrative Services, Surface Water Quality Division

Item: 4.b.

Management Views: DEQ agrees with the finding.

Again, given the timing of the previous Single Audit, fiscal year 1999-2000 was the earliest that corrective action could be implemented.

Corrective Action: In May 2000, the Environmental Assistance Division began the implementation of a cost methodology to base the allocation of administrative staff time on the actual hours that nonadministrative staff work on grants. On a quarterly basis, a comparison is made of allocated administrative staff time to the actual time worked by nonadministrative staff on various federal awards. Adjustments are made to the budgeted administrative staff allocations so that the costs recorded reflect actual time worked by nonadministrative staff.

Anticipated Completion Date: May 2000

Responsible Individual: Karen Best, Chief, Administration Section, Environmental Assistance Division

Finding Number: 760005

Finding Title: Personnel and Payroll Functions

See Finding 760001 with the findings related to the financial statements and schedules.

Glossary of Acronyms and Terms

<i>CFDA</i>	<i>Catalog of Federal Domestic Assistance.</i>
CNTL	A transaction code that provides three sections of daily operator statistics and update transaction activity: entry transaction count, transaction updates by other agencies, and batch input error list.
CRF	Cleanup and Redevelopment Subfund.
CRTF	Cleanup and Redevelopment Trust Subfund.
DEQ	Department of Environmental Quality.
DMB	Department of Management and Budget.
DNR	Department of Natural Resources.
Drinking Water State Revolving Fund (DWSRF)	A fund established within the Michigan Municipal Bond Authority to provide loans and other types of financial assistance to eligible public water systems.
DWRPD	Drinking Water and Radiological Protection Division.
DWSRF Program	The federal grant program that provides capitalization grants to states for establishing revolving funds to be used for the construction of drinking water systems in compliance with the Safe Drinking Water Act.
EPA	U.S. Environmental Protection Agency.
ERF	Environmental Response Fund.
financial audit	An audit that is designed to provide reasonable assurance about whether the financial statements and schedules of an

audited entity are fairly presented in conformity with generally accepted accounting principles.

internal control

A process, effected by an entity's management and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories: (a) reliability of financial reporting, (b) effectiveness and efficiency of operations, and (c) compliance with applicable laws and regulations.

low-risk auditee

As provided for in OMB Circular A-133, an auditee that may qualify for reduced federal audit coverage if it receives an annual Single Audit and it meets other criteria related to prior audit results. In accordance with State statute, this Single Audit was conducted on a biennial basis; consequently, this auditee is not considered a low-risk auditee.

MAIN

Michigan Administration Information Network.

material noncompliance

Violations of laws and regulations that could have a direct and material effect on major federal programs or on financial statement or schedule amounts.

material weakness

A 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 either misstatements in amounts that would be material in relation to the financial statements and/or schedules being audited or noncompliance with applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major 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.

mission

The agency's main purpose or the reason the agency was established.

MMBA

Michigan Municipal Bond Authority.

MUSTFA	Michigan Underground Storage Tank Financial Assurance.
OMB	U.S. Office of Management and Budget.
PE-110 report	PPRISM biweekly transaction report.
PPRISM	Personnel-Payroll Information System for Michigan.
PSWU	A transaction code to change, delete, and update passwords for PPRISM users.
qualified opinion	An auditor's opinion in which the auditor identifies a scope limitation or one or more instances of misstatements that impact the fair presentation of the financial statements and/or schedules in conformity with generally accepted accounting principles or an auditor's opinion in which the auditor expresses reservations about the audited agency's compliance, in all material respects, with the cited requirements that are applicable to each major federal program.
questioned costs	Costs tentatively identified as unallowable, undocumented, unapproved, or unreasonable. These costs are subject to disallowance by the federal government.
reportable condition	A matter coming to the auditor's attention relating to a significant deficiency in the design or operation of internal control that, in the auditor's judgment, could adversely affect DEQ's ability to (1) record, process, summarize, and report financial data consistent with the assertions of management in the financial statements and schedules or (2) administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants.
Single Audit	A financial audit, performed in accordance with the Single Audit Act Amendments of 1996, that is designed to meet the

needs of all federal grantor agencies and other financial report users. In addition to performing the audit in accordance with the requirements of generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, a Single Audit requires the assessment of compliance with requirements that could have a direct and material effect on a major federal program and the consideration of internal control over compliance in accordance with OMB Circular A-133.

SOMCAFR

State of Michigan Comprehensive Annual Financial Report.

SRF Program

The federal grant program that provides capitalization grants to states for establishing revolving funds to be used for the construction of municipal waste water treatment projects or for the development and implementation of nonpoint source or estuary conservation management programs and plans in compliance with the Clean Water Act.

State Revolving Fund (SRF)

A fund established within the Michigan Municipal Bond Authority to provide low-interest loans to municipalities for the construction of publicly owned water pollution control facilities.

unqualified opinion

An auditor's opinion in which the auditor states, without reservation, that the financial statements and/or schedules are fairly presented in conformity with generally accepted accounting principles or an auditor's opinion in which the auditor states, without reservation, that the audited agency complied, in all material respects, with the cited requirements that are applicable to each major federal program.