

An Audit

Petroleum Inspection Fee Revenue Obligations Program

2005-2006 Joint Legislative Audit Committee Members

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State Auditor - Janice Mueller

Audit Prepared by

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CONTENTS

Letter of Transmittal	1
Audit Opinion	3
Independent Auditor's Report on the Statement of Changes in Program Assets of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program	
Management's Discussion and Analysis	5
Financial Statement	
Statement of Changes in Program Assets for the Fiscal Years Ended June 30, 2005 and 2004	13
Notes to the Statement of Changes in Program Assets	15
Report on Control and Compliance	25
Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on Audits of the Financial Statement Performed in Accordance with Government Auditing Standards	



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Janice Mueller
State Auditor

November 11, 2005

Senator Carol A. Roessler and
Representative Suzanne Jeskewitz, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Roessler and Representative Jeskewitz:

At the request of the departments of Commerce and Administration, and in accordance with s. 13.94(1s), Wis. Stats., we have completed a financial audit of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program for the fiscal years ending June 30, 2005, and June 30, 2004. We express our unqualified audit opinion on the Statement of Changes in Program Assets and related notes.

Under the Petroleum Inspection Fee Revenue Obligations Program, the State issues revenue obligations, such as bonds and commercial paper, to provide financing for payment of claims under the Petroleum Environmental Cleanup Fund Award (PECFA) program. The obligations are not general obligation debt of the State. Instead, the revenue obligations are to be repaid primarily from the fee charged to suppliers for petroleum products sold in Wisconsin and collected by the Department of Revenue. This fee, which is established in s. 168.12(1), Wis. Stats., has been \$0.03 per gallon since before the revenue obligations program was established in January 2000, and it will remain in effect through April 30, 2006.

As provided for in 2005 Wisconsin Act 25, the petroleum inspection fee will be reduced to \$0.02 per gallon effective May 1, 2006, which will result in a decline in the petroleum inspection fee revenues available to fund debt service for the revenue obligations. While the ratings for the petroleum inspection fee revenue bonds remain unchanged, one bond rating agency recently revised its long-term rating outlook from stable to negative. Nevertheless, the Department of Administration expects that future petroleum inspection fee revenues will be sufficient to fully meet debt service requirements.

We appreciate the courtesy and cooperation extended to us during the audit by staff of the departments of Commerce, Administration, and Revenue.

Respectfully submitted,

Janice Mueller
State Auditor

JM/BN/ss

Audit Opinion ■

Independent Auditor's Report on the Statement of Changes in Program Assets of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program

We have audited the accompanying Statement of Changes in Program Assets of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program for the years ended June 30, 2005, and June 30, 2004. This financial statement is the responsibility of the program's management. Our responsibility is to express an opinion on the financial statement based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statement is free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statement. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the Statement of Changes in Program Assets presents only the Petroleum Inspection Fee Revenue Obligations Program and does not purport to, and does not, present fairly the financial position of the State of Wisconsin and the changes in its financial position and its cash flows, where applicable, in conformity with accounting principles generally accepted in the United States of America.


As described in Note 2, to provide a meaningful presentation to bondholders and noteholders regarding resources available to pay debt service, the program's policy is to prepare its financial statement on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States of America.

In our opinion, the Statement of Changes in Program Assets presents fairly, in all material respects, the Petroleum Inspection Fee Revenue Obligations Program's assets as of June 30, 2005, and June 30, 2004, and the program's receipts and disbursements for the fiscal years then ended, on the cash basis of accounting.

Our audits were conducted for the purpose of forming an opinion on the Statement of Changes in Program Assets of the Petroleum Inspection Fee Revenue Obligations Program. The supplementary information included as Management's Discussion and Analysis on pages 5 through 10 is presented for purposes of additional analysis and is not a required part of the Statement of Changes in Program Assets. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the supplementary information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 8, 2005, on our consideration of the program's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audits.

November 8, 2005

LEGISLATIVE AUDIT BUREAU
by 
Bryan Naab
Audit Director

Management's Discussion and Analysis ■

Prepared by Management of the Petroleum Inspection Fee Revenue Obligations Program

Management's Discussion and Analysis (MD&A) is intended to provide users of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program's Statement of Changes in Program Assets with a narrative overview of the statement, as well as an analysis of some key data presented in the statement. The MD&A should be read in conjunction with the accompanying financial statement and notes. The financial statement, notes, and this discussion are the responsibility of the program's management.

Overview of the Statement of Changes in Program Assets

The Statement of Changes in Program Assets of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program is intended to show the changes in the program's assets for fiscal years (FYs) 2004-05 and 2003-04. Accounting for the program is done outside the State of Wisconsin's central accounting system.

The Statement of Changes in Program Assets presents the program's receipts and disbursements on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States. Under the cash basis of accounting, receipts are recorded when received and disbursements are recorded when paid. The financial position and activity of the program is presented on the cash basis of accounting to provide a meaningful presentation to bondholders and extendible municipal commercial paper

noteholders regarding resources available to pay debt service. The notes to the financial statement provide additional information that is essential for a full understanding of the data provided in the financial statement.

Noteworthy Financial Activity

The program originated in January 2000 pursuant to a State of Wisconsin Building Commission program resolution adopted on January 19, 2000, amended and restated on May 2, 2000, and further amended on July 30, 2003. The purpose of the program is to provide financing for the payment of claims under the State of Wisconsin Petroleum Environmental Cleanup Fund Award (PECFA) program, which is administered by the Wisconsin Department of Commerce. The Building Commission may from time to time adopt supplemental resolutions authorizing the issuance of revenue obligations and revenue refunding obligations.

The program resolution establishes special trust funds and accounts and fiduciary responsibilities that are to be undertaken by a trustee for the benefit of the bondholders, extendible municipal commercial paper noteholders, and holders of any other obligations that may be issued. The Bank of New York has been appointed as the trustee for the revenue obligations. The trustee is responsible for maintaining the trust funds in accordance with the program resolution, which requires investments of trust fund balances to be in accordance with directives established by the program resolution.

As shown in Table A, the program's assets as of June 30, 2005, and June 30, 2004, were \$26.6 million and \$27.6 million, respectively, and were invested as follows:

Table A
Program Assets

	June 30, 2005	June 30, 2004	Change
Program Assets Reserved for Debt Service:			
Demand deposits	\$26,444,512	\$19,034,145	38.9%
Investments	128,400	4,104,816	-96.9
Total	26,572,912	23,138,961	14.8
Unreserved Program Assets:			
Demand deposits	6,093	4,503,281	-99.9
Total Program Assets, June 30	<u>\$26,579,005</u>	<u>\$27,642,242</u>	-3.8

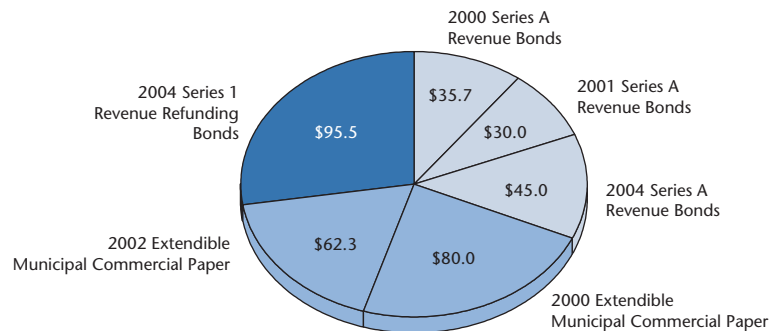
The program's revenue obligations are issued pursuant to Subchapter II of Chapter 18, Wis. Stats.; s. 101.143(9m), Wis. Stats.; and the program resolution and supplemental resolutions adopted by the State of Wisconsin Building Commission. The revenue obligations are payable from, and primarily secured by, petroleum inspection fees, as received by the trustee, that suppliers are charged on all petroleum products received for sale in Wisconsin. The revenue obligations are not general obligations of the State of Wisconsin.

During FY 2004-05, no additional bonds or extendible municipal commercial paper were issued. During FY 2003-04, \$45.0 million of revenue bonds were issued to pay PECFA claims. As of June 30, 2005, a total of \$387.6 million of revenue obligations had been issued under the program resolution and the supplemental resolutions to pay PECFA claims, to pay issuance or administrative expenses, to make deposits to reserve funds, or to pay accrued or capitalized interest. In addition, during FY 2003-04, the State issued \$95.5 million of revenue refunding bonds for the advanced refunding of previously issued revenue obligations. Statutes do not limit the amount of refunding bonds that may be issued.

A portion of the revenue bonds issued has already been repaid, and as of June 30, 2005, the total revenue obligations outstanding, excluding those bonds that were defeased as a result of the advance refunding, were \$348.5 million, consisting of \$110.7 million of revenue bonds, \$95.5 million of revenue refunding bonds, and \$142.3 million of extendible municipal commercial paper. Figure A displays the breakdown of the obligations outstanding as of June 30, 2005, by type (revenue bond or commercial paper) and series.

Figure A

**Petroleum Inspection Fee Revenue Obligations Outstanding as of June 30, 2005
(In Millions)**



As noted, \$95.5 million of refunding bonds was issued in FY 2003-04 for the advance refunding of previously issued and outstanding revenue bonds. The proceeds from the refunding bonds were deposited with an escrow agent in a separate escrow account. The refunding bond proceeds are invested by the escrow agent in United States Treasury obligations so that sufficient funds will be available to pay the principal, interest, and redemption price of the refunded bonds as they become due. The refunded bonds are not included in the outstanding revenue bonds, and the related securities in the escrow account are not included in the program's cash and investments. As a result of the advance refunding, the program effectively reduced its aggregate debt service payments by \$4.8 million over the life of the refunding bonds, as shown in Table B.

Table B

Savings Achieved from FY 2003-04 Bond Refunding
(In Millions)

	Principal	Interest	Total
2000 Series A Revenue Bonds that Were Defeased	\$96.6	\$30.1	\$126.7
Less:			
2004 Series 1 Revenue Refunding Bonds Issued	95.5	26.4	121.9
Total Savings	<u>\$ 1.1</u>	<u>\$ 3.7</u>	<u>\$ 4.8</u>

The debt service coverage ratio, calculated as the ratio of petroleum inspection fees remitted by the State to the trustee divided by the senior debt service payments made during each fiscal year, was 4.41 in FY 2004-05 and 4.95 in FY 2003-04. The ratios were based on \$26,290,295 and \$23,577,360 of total senior debt service and \$115,900,632 and \$116,635,054 of petroleum inspection fees remitted by the State to the trustee, respectively, in each of those years.

Petroleum inspection fees not retained by the trustee for debt service are transferred to the State by the trustee and are used up to the amount authorized by statute to pay PECFA claims, PECFA administrative costs, and other costs and transfers. The petroleum inspection fees transferred to the State were \$86,353,543 in FY 2004-05 and \$92,169,743 in FY 2003-04, as shown in Table C.

Table C

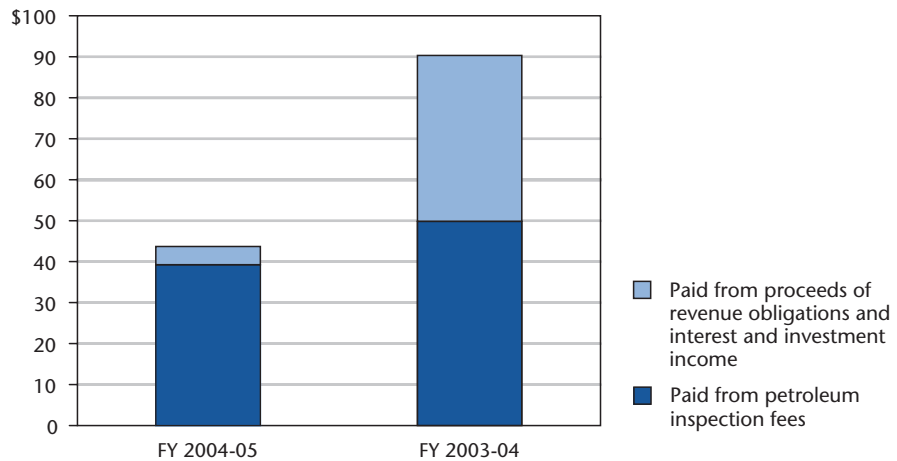
Petroleum Inspection Fees

	FY 2004-05	FY 2003-04	Change
Petroleum Inspection Fees Remitted by the State to the Trustee	\$115,900,632	\$116,634,054	-0.6%
Petroleum Inspection Fees Retained by the Trustee	29,547,089	24,464,311	20.8
Petroleum Inspection Fees Transferred by the Trustee to the State	<u>\$ 86,353,543</u>	<u>\$ 92,169,743</u>	-6.3

During FY 2004-05, \$39.2 million of claims was paid from petroleum inspection fees. This amount represents a decrease of 21.3 percent from the \$49.8 million paid from the fees in FY 2003-04 and is the result of an unanticipated decline in claims volume. In addition, \$4.5 million and \$40.5 million of claims were paid from the proceeds of revenue obligations and interest and investment income during FY 2004-05 and FY 2003-04, respectively. Figure B shows the funding of PECFA claims paid in FY 2004-05 and FY 2003-04.

Figure B

**Petroleum Environmental Cleanup Fund Award Claims Paid
(In Millions)**



The Department of Commerce has continued to reduce the amount of approved but unpaid PECFA claims. As of June 30, 2005, approved but unpaid claims were \$2.7 million, which is \$1.2 million less than at June 30, 2004.

In addition to the \$2.7 million in approved claims waiting for payment as of June 30, 2005, approximately \$7.4 million of claims submitted to the Department had yet to be both reviewed and approved. The Department estimates there were approximately \$41.0 million of additional claims that had not been submitted as of June 30, 2005, for costs that landowners had already incurred as of that date. In addition, the Department estimates that an additional \$1.2 million in liabilities may exist related to claimants appealing the Department's determinations on previously finalized claims.

On July 25, 2005, the Governor signed the budget bill into law as 2005 Wisconsin Act 25. 2005 Wisconsin Act 25 amends s. 168.12(1), Wis. Stats., by reducing the petroleum inspection fee—which is the primary source of payment for the petroleum inspection fee revenue obligations—from \$0.03 per gallon to \$0.02 per gallon effective May 1, 2006. Had a petroleum inspection fee of \$0.02 per gallon been in effect during FYs 2004-05 and 2003-04, the amounts of petroleum fees collected for each year would have been approximately two-thirds of the amounts shown in Note 8 to the financial statement, or about \$77.3 million and \$77.7 million, respectively.

On September 1, 2005, Standard and Poor's Rating Services, one of three rating agencies that have assigned ratings to the State of Wisconsin's petroleum inspection fee revenue obligations, revised its long-term rating outlook on the bonds from stable to negative. The rationale for this change was the impairment of pledged petroleum inspection fee revenues due to the reduction in the per gallon fee included in 2005 Wisconsin Act 25, resulting in reduced coverage of debt service. Standard and Poor's affirmed its "AA-" long-term rating on the petroleum inspection fee revenue bonds.

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Financial Statement ■

Statement of Changes in Program Assets for the Fiscal Years Ended June 30, 2005 and 2004

	<u>Fiscal Year 2004-05</u>	<u>Fiscal Year 2003-04</u>
Program Assets, July 1	\$ 27,642,242	\$ 19,484,638
RECEIPTS		
Proceeds from Sale of Bonds (see Note 5)	0	47,943,973
Proceeds from Sale of Extendible Municipal Commercial Paper (see Note 5)	0	0
Proceeds from Sale of Refunding Bonds (see Notes 5 and 6)	0	103,233,027
Petroleum Inspection Fees Remitted by the State of Wisconsin to the Trustee (see Note 8)	\$ 115,900,632	\$ 116,634,054
Less: Petroleum Inspection Fees Transferred from the Trustee to the State of Wisconsin Petroleum Inspection Fund (see Note 8)	<u>(86,353,543)</u>	<u>(92,169,743)</u>
Petroleum Inspection Fees Retained by the Trustee	29,547,089	24,464,311
Interest and Investment Income	<u>297,352</u>	<u>63,156</u>
Total Receipts	<u>29,844,441</u>	<u>175,704,467</u>
TOTAL PROGRAM ASSETS AVAILABLE	<u>57,486,683</u>	<u>195,189,105</u>
DISBURSEMENTS		
Transfers of Proceeds from Sale of Revenue Obligations and Interest and Investment Income to the State of Wisconsin Petroleum Inspection Fund (see Notes 1 and 10)	4,470,776	40,500,750
Transfer of Proceeds from Refunding Bonds to Escrow (see Note 6)	0	101,965,442
Debt Service (see Note 5):		
Senior debt service—bond principal	12,735,000	12,070,000
Senior debt service—bond interest	11,186,846	10,139,115
Senior debt service—commercial paper interest	2,368,449	1,368,245
Junior subordinate debt service—commercial paper principal	<u>0</u>	<u>0</u>
Total Debt Service	26,290,295	23,577,360
Debt Issuance Costs	28,459	1,388,031
Other Costs	<u>118,148</u>	<u>115,280</u>
Total Disbursements	<u>30,907,678</u>	<u>167,546,863</u>
Program Assets Reserved for Debt Service (see Note 4)	26,572,912	23,138,961
Unreserved Program Assets (see Note 4)	<u>6,093</u>	<u>4,503,281</u>
PROGRAM ASSETS, JUNE 30	<u>\$ 26,579,005</u>	<u>\$ 27,642,242</u>

The accompanying notes are an integral part of this statement.

Notes to the Statement of Changes in Program Assets ■

1. DESCRIPTION OF THE PROGRAM

The State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program, which is administered jointly by the Wisconsin Department of Commerce and the Wisconsin Department of Administration, originated in January 2000, pursuant to the State of Wisconsin Building Commission Program Resolution for State of Wisconsin Petroleum Inspection Fee Revenue Obligations, adopted on January 19, 2000, and amended and restated on May 2, 2000, and as further amended on July 30, 2003. The Building Commission may from time to time adopt supplemental resolutions authorizing the issuance of revenue obligations and revenue refunding obligations. The purpose of the program is to provide financing for the payment of claims under the State of Wisconsin Petroleum Environmental Cleanup Fund Award (PECFA) program, which is administered by the Wisconsin Department of Commerce.

The program resolution establishes special trust funds and accounts and fiduciary responsibilities that are to be undertaken by a trustee for the benefit of the bondholders, extendible municipal commercial paper noteholders, and holders of any other obligations that may be issued. The Bank of New York has been appointed as the trustee for the revenue obligations. The trustee is responsible for maintaining the trust funds in accordance with the program resolution, which requires investments of trust fund balances to be in accordance with directives established by the program resolution. The Bank of New York is also the registrar for the revenue obligations. In addition, The Bank of New York is the issuing and paying agent for revenue bonds; U.S. Bank Trust National Association is the issuing and paying agent for extendible municipal commercial paper.

Revenue bond and extendible municipal commercial paper proceeds are held by the trustee until the Department of Commerce and the Department of Administration request the trustee to remit specific amounts to the State to pay PECFA claims.

The petroleum inspection fee revenue obligations are payable from, and primarily secured by, petroleum inspection fees that result from a \$0.03 per gallon fee charged suppliers during FY 2004-05 and FY 2003-04 for petroleum products received for sale in Wisconsin (see also Note 11). These petroleum inspection fees are paid monthly by suppliers to the Wisconsin Department of Revenue, which subsequently forwards the fees to the program's trustee. All revenues and assets of the program are restricted for the purposes provided by the program resolution under which the revenue obligations are issued. The trustee transfers fees in excess of the amount needed to meet debt service requirements and pay Petroleum Inspection Fee Revenue Obligations Program administrative costs to the State of Wisconsin Petroleum Inspection Fund. The Department of Commerce uses the transferred fees to pay PECFA claims, PECFA program administrative costs, and other costs and transfers.

The Statement of Changes in Program Assets presents only the Petroleum Inspection Fee Revenue Obligations Program and is not intended to present fairly the financial activity of the State of Wisconsin.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Statement of Changes in Program Assets presents the Petroleum Inspection Fee Revenue Obligations Program's receipts and disbursements on the cash basis of accounting, which is a comprehensive basis of accounting other than accounting principles generally accepted in the United States. Under the cash basis of accounting, receipts are recorded when received and disbursements are recorded when paid. The program's assets may include cash, consisting of demand deposits held by The Bank of New York and U.S. Bank Trust National Association, and investments. The financial position and activity of the program is presented on the cash basis of accounting to provide a meaningful presentation to bondholders and extendible municipal commercial paper noteholders regarding resources available to pay debt service.

3. DEPOSITS AND INVESTMENTS

The program's deposit and investment policies are governed by Wisconsin Statutes and the program resolution. The program is authorized by statutes and the program resolution to deposit funds with the trustee and the commercial paper issuing and paying agent. The program is also authorized by statutes and the program resolution to invest funds reserved for debt service in direct obligations of the United States. In addition, the program is

authorized to invest funds not reserved for debt service in direct obligations of the United States; high-quality corporate commercial paper; certificates of deposit; and other investments authorized under s. 25.17(3)(b), Wis. Stats., and permitted by the program resolution.

As of June 30, 2005, the demand deposit accounts with the trustee and the commercial paper issuing and paying agent totaled \$26,450,605. As of June 30, 2004, the demand deposit accounts with the trustee and the commercial paper issuing and paying agent totaled \$23,537,426. Each year, \$200,000 was insured against loss by the Federal Deposit Insurance Corporation. The remaining \$26,250,605 as of June 30, 2005, and \$23,337,426 as of June 30, 2004, were not insured or collateralized.

As of June 30, 2005, the program held investments, purchased for \$128,400, consisting of U.S. Treasury Notes with a face value of \$128,000. These investments were registered and held by the program's agent in the program's name. As of June 30, 2005, these investments had a fair market value of \$127,035, and they are scheduled to mature on December 31, 2005.

As of June 30, 2004, the program held investments purchased for \$4,104,816 consisting of U.S. Treasury Notes with a face value of \$4,117,000. These investments were registered and held by the program's agent in the program's name. As of June 30, 2004, the total fair market value of these investments was \$4,094,695, of which investments valued at \$3,967,775 were scheduled to mature on or before June 30, 2005, and investments valued at \$126,920 were scheduled to mature on December 31, 2005.

4. PROGRAM ASSETS

Program assets required to be held in the various interest and principal redemption accounts at the trustee and the issuing and paying agents are reported as Program Assets Reserved for Debt Service. Program assets in excess of those reserved for debt service are reported as Unreserved Program Assets. The program's unreserved assets are available for transfer to the State of Wisconsin Petroleum Inspection Fund to pay PECFA claims, debt issuance costs, or administrative costs of the program.

As of June 30, 2005, the program's assets totaled \$26,579,005. Of this amount, \$26,572,912, consisting of demand deposits of \$26,444,512 and investments acquired for \$128,400, was reserved for debt service. The remaining \$6,093, consisting of demand deposits, was unreserved.

As of June 30, 2004, the program's assets totaled \$27,642,242. Of this amount, \$23,138,961, consisting of demand deposits of \$19,034,145 and investments acquired for \$4,104,816, was reserved for debt service. The remaining \$4,503,281, consisting of demand deposits, was unreserved.

5. REVENUE BONDS AND EXTENDIBLE MUNICIPAL COMMERCIAL PAPER

The program’s revenue obligations are issued pursuant to Subchapter II of Chapter 18, Wis. Stats.; s. 101.143(9m), Wis. Stats.; and the program resolution and supplemental resolutions adopted by the State of Wisconsin Building Commission. The revenue obligations are payable from, and primarily secured by, petroleum inspection fees that suppliers are charged on all petroleum products received for sale in Wisconsin (see also Notes 8 and 11). The revenue obligations are not general obligations of the State.

Excluding any bonds that were defeased as a result of the issuance of the advance refunded bonds (see Note 6), the senior revenue bonds issued by the program and outstanding as of June 30, 2005, were as follows:

Senior Revenue Bonds

<u>Date Issued</u>	<u>Series</u>	<u>Interest Rates</u>	<u>Interest Payable</u>	<u>Maturity Through</u>	<u>Amount Issued</u>	<u>June 30, 2005 Amount Outstanding</u>
03/02/2000	2000 Series A	5.25 to 6.0%	Semiannually on 1/1 and 7/1	07/01/2012	\$170,250,000	\$ 35,685,000
12/18/2001	2001 Series A	5.0	Semiannually on 1/1 and 7/1	07/01/2008	30,000,000	30,000,000
02/04/2004	2004 Series A	3.0 to 5.0	Semiannually on 1/1 and 7/1	07/01/2012	45,000,000	45,000,000
05/20/2004	2004 Series 1	3.0 to 5.0	Semiannually on 1/1 and 7/1	07/01/2012	<u>95,470,000</u>	<u>95,470,000</u>
Total Senior Revenue Bonds					<u>\$340,720,000</u>	<u>\$206,155,000</u>

The 2000 Series A Petroleum Inspection Fee Revenue Bonds maturing on or after July 1, 2006, are subject to optional redemption on or after July 1, 2005, at prices ranging from 102 to 100 percent of the face value plus accrued interest. The 2001 Series A Petroleum Inspection Fee Revenue Bonds are subject to optional redemption on or after July 1, 2006, at a price of 100 percent of the face value plus accrued interest. The 2004 Series A Petroleum Inspection Fee Revenue Bonds maturing on or after July 1, 2010, are subject to optional redemption on or after July 1, 2009, at prices ranging from 102 to 100 percent of the face value plus accrued interest. The 2004 Series 1 Petroleum Inspection Fee Revenue Refunding Bonds, maturing on or after July 1, 2010, are subject to optional redemption on or after July 1, 2009, at prices ranging from 102 to 100 percent of the face value plus accrued interest.

During the fiscal years ended June 30, the following changes occurred in revenue bonds outstanding:

<u>Fiscal Year</u>	<u>Balance July 1</u>	<u>Bonds Issued</u>	<u>Principal Repaid or Defeased</u>	<u>Balance June 30</u>
FY 2003-04	\$187,060,000	\$140,470,000	\$108,640,000	\$218,890,000
FY 2004-05	218,890,000	0	12,735,000	206,155,000

As of June 30, 2005, the program's future debt service requirements for principal and interest for Petroleum Inspection Fee Revenue Bonds 2000 Series A, 2001 Series A, 2004 Series A, and 2004 Series 1 are as follows:

Future Debt Service on Revenue Bonds

<u>Fiscal Year Ending June 30</u>	<u>Principal Amount</u>	<u>Interest Amount</u>	<u>Total Debt Service on Bonds</u>
2006	\$ 18,205,000	\$ 9,581,888	\$ 27,786,888
2007	19,775,000	8,596,081	28,371,081
2008	35,270,000	7,230,000	42,500,000
2009	36,280,000	5,494,500	41,774,500
2010	22,350,000	4,056,025	26,406,025
2011	23,470,000	2,940,600	26,410,600
2012	24,635,000	1,799,625	26,434,625
2013	<u>26,170,000</u>	<u>607,663</u>	<u>26,777,663</u>
Total	\$206,155,000	\$40,306,382	\$246,461,382

The program may also issue extendible municipal commercial paper, which may have maturities from 1 to 180 days and is not callable prior to maturity. The principal of and interest on the extendible municipal commercial paper will be paid at maturity unless the State exercises its option to extend the maturity date to a date that is up to 270 days after the original issue date. New (rollover) extendible municipal commercial paper may be issued to pay the principal due on maturing extendible municipal commercial paper. Each note bears interest from its date of issuance, at the rate determined on the date of issuance.

Interest payments on extendible municipal commercial paper are on a parity with the payments on the senior bonds. Principal on extendible municipal commercial paper has a junior subordinate pledge and is payable from proceeds of rollover notes, issuance of refunding senior bonds, certain moneys held by the trustee, or other funds made available by the State for this purpose.

The following table presents the extendible municipal commercial paper activity for FY 2003-04 and FY 2004-05.

<u>Fiscal Year</u>	<u>Balance July 1</u>	<u>Commercial Paper Issued</u>	<u>Principal Repaid</u>	<u>Balance June 30</u>
FY 2003-04	\$142,300,000	\$0	\$0	\$142,300,000
FY 2004-05	142,300,000	0	0	142,300,000

As of June 30, 2005, the \$142,300,000 in outstanding extendible municipal commercial paper had interest rates ranging from 2.48 percent to 2.95 percent, and maturities ranging from July 7, 2005, to August 10, 2005. As of June 30, 2004, the \$142,300,000 in outstanding extendible municipal commercial paper had interest rates ranging from 1.06 percent to 1.13 percent, and maturities ranging from August 10, 2004, to September 8, 2004.

Additional series of senior bonds may be issued on parity with the current bond series outstanding and collateralized by an equal lien on the petroleum inspection fees. However, no additional series, other than refunding bonds and bonds issued to fund outstanding extendible municipal commercial paper, may be issued unless, among other things, the debt service coverage ratio, as defined in the program resolution, is at least 2.0.

Each month that variable-rate debt, such as the extendible municipal commercial paper, is outstanding, the State is required by the program resolution to provide to the trustee a certificate setting forth the program's "variable rate takeout capacity" and "variable rate debt exposure." The "variable rate takeout capacity" measures the State's ability, given certain conservative interest rate assumptions, to convert variable-rate debt to fixed-rate debt. "Variable rate debt exposure" measures the program's outstanding variable-rate debt. This certification was required and performed each month during FY 2004-05 and FY 2003-04. Because the program's ability to convert variable-rate debt to fixed-rate debt was higher than the amount of variable-rate debt outstanding each month, as evidenced by the program's variable-rate takeout capacity, the State needed to take no further action. For June 2005, the program's variable-rate takeout capacity was calculated to be \$399,880,323, which was \$257,580,323 higher than the variable-rate debt exposure of \$142,300,000. For June 2004, the program's variable-rate takeout capacity was calculated to be \$383,559,344, which was \$241,259,344 higher than the variable-rate debt exposure of \$142,300,000.

6. ADVANCE REFUNDING

On May 20, 2004, the program issued \$95,470,000 of 2004 Series 1 Revenue Refunding Bonds, the proceeds of which were deposited in an escrow account to provide for the advance refunding of \$96,570,000 of the program's 2000 Series A Revenue Bonds. Refunding bond proceeds in the amount of \$101,965,442 have been invested by the escrow agent in United States Treasury obligations so that sufficient monies will be available to pay the principal, interest, and redemption price of the refunded bonds. As a result, \$96,570,000 of the program's 2000 Series A Revenue Bonds are considered to be defeased, and the refunded bonds are not included in the revenue bonds outstanding as of June 30, 2005, or as of June 30, 2004, as summarized in Note 5, and the related securities in the escrow account are not included in the Program Assets as of June 30, 2005 or as of June 30, 2004. As a result of the advance refunding, the program effectively reduced its aggregate debt service payments by \$4.8 million over the life of the refunding bonds and obtained an economic gain of \$4.0 million.

The revenue bonds defeased by the 2004 Series 1 refunding revenue bonds that remain outstanding as of June 30, 2005, are as follows:

<u>Series</u>	<u>Maturity</u>	<u>Principal Amount</u>	<u>Redemption Date</u>	<u>Redemption Price</u>
2000 Series A	July 1, 2007	\$15,115,000	July 1, 2005	102%
2000 Series A	July 1, 2008	15,980,000	July 1, 2005	102%
2000 Series A	July 1, 2009	16,885,000	July 1, 2005	102%
2000 Series A	July 1, 2010	17,800,000	July 1, 2005	102%
2000 Series A	July 1, 2011	18,790,000	July 1, 2005	102%
2000 Series A	July 1, 2012	<u>12,000,000</u>	July 1, 2005	102%
Total Refunded Bonds		\$96,570,000		

7. DEBT AUTHORITY FOR THE PROGRAM

In addition to the petroleum inspection fee revenue obligations issued through June 30, 2005, Wisconsin Statutes and the State of Wisconsin Building Commission have authorized the program to issue additional revenue obligations of up to \$49,076,000, plus an additional amount not to exceed \$924,000 to pay issuance and administrative costs, make any necessary deposits to reserve funds, or pay accrued or capitalized interest. Further, the Building Commission has authorized the program to issue revenue bonds to fund any or all of the outstanding extendible municipal commercial paper and to issue up to \$71,150,000 in revenue refunding bonds to refund currently outstanding bonds, plus an additional amount not to exceed \$1,450,000 to pay issuance and administrative costs, make any necessary deposits to reserve funds, or pay accrued or capitalized interest.

8. PETROLEUM INSPECTION FEES

Petroleum inspection fees result from the fees imposed under s. 168.12(1) Wis. Stats., and payments received under ss. 101.143(4)(h)1m, 101.143(5)(a), and 101.143(5)(c), Wis. Stats. Under s. 168.12(1), Wis. Stats., a \$0.03 per gallon fee was imposed by the State on suppliers for all petroleum products received for sale in Wisconsin during FY 2004-05 and FY 2003-04 (see also Note 11). The fees are paid to the State of Wisconsin Department of Revenue by suppliers along with motor fuel taxes. The Department of Revenue determines the amount collected for the fees and remits it to the program’s trustee on a monthly basis. For certain months during FY 2004-05 and FY 2003-04, the Department of Revenue transferred \$8.8 million to the trustee and made adjustments in subsequent months when actual collections became known. The other petroleum inspection fees consist of penalty payments made under s. 101.143(4)(h)1m, Wis. Stats., by consultants for submitting claims for ineligible costs; proceeds under s. 101.143(5)(a), Wis. Stats., from the sale of remedial equipment and supplies that had originally been paid for by PECFA awards; and net recoveries under s. 101.143(5)(c), Wis. Stats., related to the Wisconsin Attorney General’s actions against fraudulent claims.

The trustee transfers the petroleum inspection fees in excess of the amount needed to meet debt service requirements and to pay Petroleum Inspection Fee Revenue Obligations Program administrative costs to the State of Wisconsin Petroleum Inspection Fund, free of the first lien pledge of the program resolution. The Department of Commerce uses the fees transferred to the State of Wisconsin Petroleum Inspection Fund to pay PECFA claims, PECFA program administrative costs, and other costs and transfers.

From July 1, 2003, through June 30, 2005, the following amounts of petroleum inspection fees were remitted by the Wisconsin Department of Revenue to the trustee, retained by the trustee to meet debt service requirements and pay Petroleum Inspection Fee Revenue Obligations Program administrative costs, and transferred by the trustee to the State of Wisconsin Petroleum Inspection Fund.

<u>Month</u>	Petroleum Inspection Fees Remitted by the State to the Trustee	Petroleum Inspection Fees Retained by the Trustee	Petroleum Inspection Fees Transferred by the Trustee to the State
July 2004	\$ 8,800,000	\$ 2,383,156	\$ 6,416,844
August	11,393,340	2,382,855	9,010,485
September	8,783,390	2,444,155	6,339,235
October	8,800,000	2,456,156	6,343,844
November	13,351,929	2,511,056	10,840,873
December	8,724,095	2,455,838	6,268,257
January 2005	9,316,866	2,449,778	6,867,088
February	10,118,832	2,441,074	7,677,758
March	10,058,425	2,432,874	7,625,551
April	8,179,391	2,457,674	5,721,717
May	9,328,603	2,427,146	6,901,457
June	<u>9,045,761</u>	<u>2,705,327</u>	<u>6,340,434</u>
Total FY 2004-05	<u>\$115,900,632</u>	<u>\$29,547,089</u>	<u>\$86,353,543</u>
July 2003	\$ 9,826,106	\$ 2,017,062	\$ 7,809,044
August	10,204,569	1,993,516	8,211,053
September	9,888,788	1,965,570	7,923,218
October	12,816,429	1,995,589	10,820,840
November	8,856,448	2,032,956	6,823,492
December	8,800,000	2,025,950	6,774,050
January 2004	8,800,000	2,031,516	6,768,484
February	8,800,000	2,060,678	6,739,322
March	11,315,333	1,983,516	9,331,817
April	8,800,000	2,006,219	6,793,781
May	9,726,381	1,981,225	7,745,156
June	<u>8,800,000</u>	<u>2,370,514</u>	<u>6,429,486</u>
Total FY 2003-04	<u>\$116,634,054</u>	<u>\$ 24,464,311</u>	<u>\$92,169,743</u>

9. DEBT SERVICE COVERAGE RATIO FOR SENIOR DEBT

There are alternative methods to calculate debt service coverage. For purposes of additional analysis, the debt service coverage ratios for senior debt for FY 2004-05 and FY 2003-04 follow. They are calculated as the ratio of petroleum inspection fees remitted to the trustee during the respective fiscal years, divided by the senior debt service payments made during each fiscal year.

Debt Service Coverage Ratio for Senior Debt

	<u>Fiscal Year 2004-05</u>	<u>Fiscal Year 2003-04</u>
Fees Remitted to the Trustee	\$115,900,632	\$116,634,054
Senior Debt Service:		
Principal—bonds	\$12,735,000	\$12,070,000
Interest—bonds	11,186,846	10,139,115
Interest—commercial paper	<u>2,368,449</u>	<u>1,368,245</u>
Total Senior Debt Service	\$ 26,290,295	\$ 23,577,360
Debt Service Coverage Ratio for Senior Debt	4.41	4.95

10. PECFA CLAIMS

The Petroleum Inspection Fee Revenue Obligations Program was established during FY 1999-2000, and bonds and extendible municipal commercial paper were issued to reduce a backlog that had accumulated because at that time approved PECFA claims significantly exceeded the petroleum inspection fee revenues available to pay the claims. While the backlog has been largely eliminated, PECFA claims continue to be submitted to the Department of Commerce, and additional bonds and extendible municipal commercial paper were issued to pay approved PECFA claims.

The following table summarizes the activity related to PECFA claims during FY 2004-05 and FY 2003-04.

**Summary of PECFA Claims
July 1, 2003 through June 30, 2005
(In Millions)**

	<u>FY 2004-05</u>	<u>FY 2003-04</u>
Approved but Unpaid PECFA Claims as of July 1	\$ 3.9	\$ 5.7
Claims Approved for Payment during the Fiscal Year	<u>42.5</u>	<u>88.5</u>
Total Approved PECFA Claims	<u>46.4</u>	<u>94.2</u>
Less Claims Paid:		
Paid from Proceeds of Revenue Obligations and Interest and Investment Income	4.5	40.5
Paid From Petroleum Inspection Fees	<u>39.2</u>	<u>49.8</u>
Total Claims Paid during the Fiscal Year	<u>43.7</u>	<u>90.3</u>
Approved but Unpaid PECFA Claims as of June 30	\$ 2.7	\$ 3.9

In addition to the \$2.7 million in approved claims waiting for payment as of June 30, 2005, approximately \$7.4 million of claims submitted to the Department of Commerce had yet to be both reviewed and approved. The Department estimates that there were approximately \$41.0 million of additional claims that had not been submitted as of June 30, 2005, for costs that landowners had already incurred as of that date. In addition, the Department estimates that an additional \$1.2 million in liabilities may exist related to claimants appealing the Department's determinations on previously finalized claims.

11. SUBSEQUENT EVENTS

On July 25, 2005, the Governor signed the budget bill into law as 2005 Wisconsin Act 25. 2005 Wisconsin Act 25 amends s. 168.12(1), Wis. Stats., by reducing the petroleum inspection fee—which is the primary source of payment for the petroleum inspection fee revenue obligations—from \$0.03 per gallon to \$0.02 per gallon, effective May 1, 2006. Had a petroleum inspection fee of \$0.02 per gallon been in effect during FYs 2004-05 and 2003-04, the amounts of petroleum fees collected for each year would have been approximately two-thirds of the amounts shown in Note 8 of this document, or about \$77.3 million and \$77.7 million, respectively.

On September 1, 2005, Standard and Poor's Rating Services, one of three rating agencies that have assigned ratings to the State of Wisconsin's petroleum inspection fee revenue obligations, revised its long-term rating outlook on the bonds from stable to negative. The rationale for this change was the impairment of pledged petroleum inspection fee revenues due to the reduction in the per gallon fee included in 2005 Wisconsin Act 25, resulting in reduced coverage of debt service. Standard and Poor's affirmed its "AA-" long-term rating on the petroleum inspection fee revenue bonds.

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Report on Control and Compliance ■

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on Audits of the Financial Statement Performed in Accordance with Government Auditing Standards

We have audited the cash-basis Statement of Changes in Program Assets of the State of Wisconsin Petroleum Inspection Fee Revenue Obligations Program for the years ended June 30, 2005, and June 30, 2004, and have issued our report thereon dated November 8, 2005. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

INTERNAL CONTROL OVER FINANCIAL REPORTING


In planning and performing our audits, we considered the program's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the Statement of Changes in Program Assets and not to provide an opinion on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statement being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the program's Statement of Changes in Program Assets is free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This independent auditor's report is intended for the information and use of the program's management and the Wisconsin Legislature. This independent auditor's report, upon submission to the Joint Legislative Audit Committee, is a matter of public record and its distribution is not limited. However, because we do not express an opinion on internal control over financial reporting or on compliance, this report is not intended to be used by anyone other than these specified parties.

November 8, 2005

LEGISLATIVE AUDIT BUREAU
by 
Bryan Naab
Audit Director