



STATE OF WISCONSIN

Notice of **Material Information** #2005-09
November 10, 2005

This document provides information which may be material to financial evaluation of the State of Wisconsin, however neither the preparation nor submission of this document constitutes a Listed Event pursuant to the State's Master Agreement on Continuing Disclosure.

Issue: State of Wisconsin
Clean Water Revenue Obligations

CUSIP Numbers: Bonds—977092 Prefix (All)

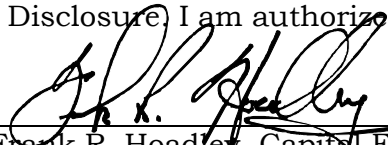
Type of Information: Audited Financial Statements for the 2005 Fiscal Year

Attached are the **audited financial statements** for the year ended June 30, 2005, for the Environmental Improvement Fund and June 1, 2005 for the Leveraged Loan Portfolio.

Type of Filing: Filed in electronic form with each Nationally Recognized Municipal Securities Information Repository through DisclosureUSA. This notice is also available on the State of Wisconsin Capital Finance web site at:

www.doa.state.wi.us/capitalfinance

The undersigned represents that he is the Capital Finance Director, State of Wisconsin Capital Finance Office, which is the office of the State of Wisconsin responsible for providing Annual Reports and Notice of Material Events when notice is required by the State's Master Agreement on Continuing Disclosure. I am authorized to distribute this information publicly.



Frank R. Hoadley, Capital Finance Director
State of Wisconsin Capital Finance Office
Wisconsin Department of Administration
101 East Wilson Street
Madison, WI 53702
Phone: (608) 266-2305
Fax: (608) 266-7645

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND
AND
LEVERAGED LOAN PORTFOLIO**

STATE OF WISCONSIN

ENVIRONMENTAL IMPROVEMENT FUND

FINANCIAL STATEMENTS
For the Years Ended June 30, 2005 and 2004,
SUPPLEMENTAL INFORMATION
For the Year Ended June 30, 2005, and
Independent Auditors' Report

AND

LEVERAGED LOAN PORTFOLIO

FINANCIAL STATEMENTS
For the Year Ended June 1, 2005 and
Independent Auditors' Report

STATE OF WISCONSIN

TABLE OF CONTENTS

ENVIRONMENTAL IMPROVEMENT FUND

INDEPENDENT AUDITORS' REPORT	1 – 2
FINANCIAL STATEMENTS	
Statements of Net Assets – June 30, 2005 and 2004	3
Statements of Revenues, Expenses, and Changes in Net Assets – Years Ended June 30 2005 and 2004	4
Statements of Cash Flows – Years Ended June 30, 2005 and 2004	5 – 6
Notes to Financial Statements	7 – 21
SUPPLEMENTAL INFORMATION	
Statement of Net Assets by Program – June 30, 2005	22 – 25
Statement of Revenues, Expenses, and Changes in Net Assets by Program – Year Ended June 30, 2005	26 – 27
Statement of Cash Flows by Program – Year Ended June 30, 2005	28 – 31
OTHER INFORMATION (UNAUDITED)	32

LEVERAGED LOAN PORTFOLIO

INDEPENDENT AUDITORS' REPORT	33
FINANCIAL STATEMENTS	
Statement of Net Assets – June 1, 2005	34
Statement of Revenues, Expenses, and Changes in Net Assets – Year Ended June 1, 2005	35
Statement of Cash Flows – Year Ended June 1, 2005	36 – 37
Notes to Financial Statements	38 – 48
OTHER INFORMATION (UNAUDITED)	49



INDEPENDENT AUDITORS' REPORT

To the Secretary of the Department of Administration
and the Secretary of the Department of
Natural Resources of the State of Wisconsin

We have audited the accompanying financial statements of the State of Wisconsin Environmental Improvement Fund, an enterprise fund of the State of Wisconsin, as of June 30, 2005, and for the year then ended as listed in the table of contents. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of the State of Wisconsin Environmental Improvement Fund as of June 30, 2004. Those financial statements were audited by other auditors whose report thereon has been furnished to us, and our opinion, insofar as it relates to the amounts included for the Environmental Improvement Fund, is based on the report of the other auditors.

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

As discussed in Note 1, the financial statements present only the State of Wisconsin Environmental Improvement Fund and are not intended to present fairly the financial position of the State of Wisconsin, and the changes in its financial position and its cash flows in conformity with accounting principles generally accepted in the United States of America.

In our opinion, based on our audit and the report of the other auditors, the financial statements referred to above present fairly, in all material respects, the financial position of the State of Wisconsin Environmental Improvement fund as of June 30, 2005 and 2004, and the changes in its financial position and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

The State of Wisconsin Environmental Improvement Fund has not presented the management's discussion and analysis that accounting principles generally accepted in the United States of America require to supplement, although not to be part of, the financial statements.

The supplemental information as identified in the table of contents is presented for purposes of additional analysis and is not a required part of the financial statements. 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.

To the Secretary of the Department of Administration
and the Secretary of the Department of
Natural Resources of the State of Wisconsin

The "Other Information" on page 32 is presented for informational purposes only and is not a required part of the financial statements of the State of Wisconsin Environmental Improvement Fund. The information has not been audited by us and, accordingly, we express no opinion on such information.

Madison, Wisconsin
October 6, 2005

Vuchow Krause + Company LLP

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENTS OF NET ASSETS
June 30, 2005 and 2004

	2005	2004
ASSETS		
Current Assets		
Unrestricted cash and cash equivalents	\$ 190,955,803	\$ 271,142,238
United States Treasury Notes, purchased in connection with forward delivery agreements, at cost	23,386,696	23,386,431
Receivables		
Loans to local governments - current portion	99,829,820	84,556,978
Due from other funds	202,202	274,990
Due from other governmental entities	7,799,927	8,262,625
Accrued investment income	329,808	329,806
Prepaid items	20,947	3,981
Total Current Assets	322,525,203	387,957,049
Noncurrent Assets		
Restricted assets - cash equivalents	72,700,346	68,576,666
Investments - State of Wisconsin general obligation clean water bonds, at fair value	145,895,768	135,016,318
Loans to local governments	1,300,881,128	1,214,028,995
Prepaid items	302,558	-
Deferred debt expense	2,826,909	2,650,182
Total Noncurrent Assets	1,522,606,709	1,420,272,161
TOTAL ASSETS	\$ 1,845,131,912	\$ 1,808,229,210
LIABILITIES AND NET ASSETS		
Current Liabilities		
Accrued expenses	\$ 192,116	\$ 239,627
Accrued interest on bonds	2,775,085	2,958,106
Due to other funds	1,885,855	1,355,109
Due to other governmental entities	472,844	187,166
Revenue obligation bonds - current maturities	44,775,000	39,340,000
Total Current Liabilities	50,100,900	44,080,008
Noncurrent Liabilities		
Revenue obligation bonds, net (including deferred charge)	607,437,777	652,771,447
Due to other governmental entities	996,824	1,470,083
Accrued expenses	30,832	31,787
Total Noncurrent Liabilities	608,465,433	654,273,317
Total Liabilities	658,566,333	698,353,325
Net Assets		
Restricted for environmental improvement	1,156,713,081	1,079,853,500
Unrestricted	29,852,498	30,022,385
Total Net Assets	1,186,565,579	1,109,875,885
TOTAL LIABILITIES AND NET ASSETS	\$ 1,845,131,912	\$ 1,808,229,210

See accompanying notes to financial statements.

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
For the Years Ended June 30, 2005 and 2004

	2005	2004
OPERATING REVENUES		
Loan interest	\$ 22,484,992	\$ 20,686,388
Interest income used as security for revenue bonds	17,674,648	17,143,708
Other	46,767	41,083
Total Operating Revenues	40,206,407	37,871,179
 OPERATING EXPENSES		
Interest	33,677,059	34,527,086
Salaries and benefits	3,598,007	5,016,264
Contractual services and other	1,348,529	1,636,767
Total Operating Expenses	38,623,595	41,180,117
 Operating Income (Loss)	1,582,812	(3,308,938)
 NONOPERATING REVENUES (EXPENSES)		
Investment income	3,914,291	1,661,164
Investment income used as security for revenue bonds	16,404,323	3,723,382
Operating grants	61,713,353	92,588,682
Hardship grants awarded	(858,753)	(1,065,392)
Total Nonoperating Revenues, Net	81,173,214	96,907,836
 INCOME BEFORE TRANSFERS	82,756,026	93,598,898
 Transfers in/(out)	(6,066,332)	32,225,210
 Increase in Net Assets	76,689,694	125,824,108
 TOTAL NET ASSETS - Beginning of Year	1,109,875,885	984,051,777
 TOTAL NET ASSETS - END OF YEAR	\$ 1,186,565,579	\$ 1,109,875,885

See accompanying notes to financial statements.

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2005 and 2004

	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES		
Payments to employees for services	\$ (3,202,225)	\$ (4,151,899)
Payments to suppliers and other	(1,691,462)	(2,740,580)
Other operating revenues (expenses)	46,767	-
Net Cash Flows From (used by) Operating Activities	(4,846,920)	(6,892,479)
 CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Operating grants received	62,489,992	91,195,049
Grants paid	(858,753)	(1,065,392)
Transfers in (out)	(6,066,332)	32,225,210
Proceeds from issuance of long-term debt	117,509,813	123,164,771
Refunding bond proceeds deposited in irrevocable trust	(117,380,148)	-
Retirement of long-term debt	(39,340,000)	(54,340,000)
Interest payments	(34,573,762)	(34,317,789)
Net Cash Flows From Noncapital Financing Activities	(18,219,190)	156,861,849
 CASH FLOWS FROM INVESTING ACTIVITIES		
Origination of loans	(190,745,993)	(181,386,392)
Collection on loans	88,621,015	79,309,508
Interest received on loans	39,845,698	37,366,550
Purchase of investments	(46,773,506)	(66,773,252)
Liquidation of investments	46,773,242	50,020,893
Increase in restricted cash equivalents	(4,123,680)	(4,442,057)
Investment and interest income	9,282,899	9,245,855
Net Cash Flows From Investing Activities	(57,120,325)	(76,658,895)
 Net Increase (Decrease) in Unrestricted Cash and Cash Equivalents	(80,186,435)	73,310,475
 CASH AND CASH EQUIVALENTS - Beginning of Year	271,142,238	197,831,763
 CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 190,955,803	\$ 271,142,238

	<u>2005</u>	<u>2004</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH FLOWS FROM OPERATING ACTIVITIES		
Operating Income (Loss)	\$ 1,582,812	\$ (3,308,938)
ADJUSTMENTS TO RECONCILE OPERATING INCOME (LOSS) TO NET CASH FLOWS FROM OPERATING ACTIVITIES		
Amortization	(647,200)	136,715
Interest income classified as investing activity	(40,159,640)	(37,830,095)
Interest expense classified as noncapital financing activity	34,507,280	34,181,075
Changes in assets and liabilities:		
Prepaid items	(319,523)	-
Other assets	-	(38)
Deferred debt expense	(151,380)	(113,503)
Due from other funds	72,787	29,115
Accrued expenses	(48,461)	100,260
Accrued interest on bonds	(183,021)	209,297
Due to other funds	530,746	(282,893)
Due to other governmental entities	(31,320)	(13,474)
Total Adjustments	<u>(6,429,732)</u>	<u>(3,583,541)</u>
NET CASH USED IN OPERATIONS	<u>\$ (4,846,920)</u>	<u>\$ (6,892,479)</u>

NONCASH INVESTING AND NONCAPITAL FINANCING ACTIVITIES: NONE

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity—The State of Wisconsin Environmental Improvement Fund (the “Fund”) is an enterprise fund of the State of Wisconsin (the “State”) administered by the State of Wisconsin Department of Natural Resources (the “DNR”) and the State of Wisconsin Department of Administration (the “DOA”).

The Fund was established with the adoption of the 1997-1999 State of Wisconsin budget. The Fund replaced the Clean Water Fund Program and expanded loan activity to include drinking water system loans and brownfield loans. The Fund provides for three separate environmental financing programs: the Clean Water Fund Program, the Safe Drinking Water Loan Program, and the Land Recycling Loan Program.

The Clean Water Fund Program was established in 1990 and provides financial assistance to municipalities at subsidized interest rates for the purpose of constructing or improving municipal wastewater facilities. The Safe Drinking Water Loan Program was established in 1997 and provides municipal loans for the construction or repair of municipal drinking water facilities. The following four loan portfolios comprise the Environmental Improvement Fund:

- **Leveraged Loan Portfolio**—This portfolio is funded by proceeds of revenue obligation bonds and operating transfers from the State. Assets in this portfolio are used for loans for Wisconsin municipal wastewater projects that meet applicable State eligibility and reporting requirements of the Clean Water Fund Program.
- **Direct Loan Portfolio**—This portfolio is funded by the U.S. Environmental Protection Agency (the “EPA”) grants and operating transfers from the State (i.e., a minimum 20% match of EPA capitalization grant). Repayments from loans in this portfolio are also used to fund new loans. Loans in this portfolio are made for wastewater projects that comply with EPA eligibility and reporting requirements of the Clean Water Fund Program.
- **Proprietary Loan/Grant Portfolio**—This portfolio is funded by operating transfers from the State. Assets of this portfolio are used to fund both loans and hardship grants for qualifying wastewater projects. Repayments from loans in this portfolio may be used to fund new loans or hardship grants under the Clean Water Fund Program.
- **Drinking Water Loan Portfolio**—This portfolio is funded by the EPA grants and operating transfers from the State (the State is required to match a minimum of 20% of EPA grants). Repayments from loans in this portfolio may be used to fund new loans. Loans in this portfolio are made for drinking water projects that comply with EPA eligibility and reporting requirements under the Safe Drinking Water Loan Program.

The Land Recycling Loan Program is a municipal loan program for the remediation of contaminated lands. There have been seven loans granted under this program for a total of \$11,666,140. As of June 30, 2005, the total amount drawn on these loans was \$10,166,000. The Land Recycling Program loans are included in the Clean Water Fund Program – Direct Loan Portfolio for reporting purposes.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

Reporting Entity (cont.)—The Fund applies all applicable Governmental Accounting Standards Board (“GASB”) pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

Net Operating Income/Loss—The Fund incurred net operating income of \$1.6 million in 2005 and a net operating loss of \$3.3 million in 2004. Management expects the Fund will generally incur net operating losses in most years. As explained in Note 2, a loss will generally result from the Fund’s statutory mission to provide loans to municipalities at interest rates below the Fund’s own cost of funds. Previous losses have historically been funded by EPA grants and operating transfers from the State of Wisconsin. EPA grants were approximately \$61.7 million and \$92.6 million in 2005 and 2004, respectively, and are classified as operating grants. Operating transfers from the State of Wisconsin were approximately \$-0- million and \$32.2 million in 2005 and 2004, respectively, and are classified as transfers in. Management expects the grants and transfers will continue for the foreseeable future sufficient to fund both the anticipated future net operating losses and, together with additional borrowing, to fund additional loans to municipalities.

Loans Receivable—Loans receivable are recorded at cost. Direct costs to originate loans are not material and are expensed as incurred. Fees received to originate loans are not material and are recorded as income when received.

Interest on Loans Receivable—Interest on loans receivable is recognized on an accrual basis and recorded within Due From Other Governmental Entities on the statements of net assets.

Investments—The Fund may invest in direct obligations of the United States and Canada, securities guaranteed by the United States, certificates of deposit issued by banks in the United States, and solvent financial institutions in the State, commercial paper and nonsecured corporation notes and bonds, bankers acceptances, participation agreements, privately placed bonds and mortgages, common and preferred stock and other securities approved by applicable sections of the Wisconsin Statutes, bond resolutions, and various trust indentures (see Note 3 to the financial statements).

United States Treasury Notes, Purchased in Connection with Forward Delivery Agreements—The Fund holds United States Treasury Notes as investments at June 30, 2005 and 2004 and records the notes at cost. The Fund purchased these securities in accordance with the Forward Delivery Agreements (see Note 4).

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

United States Treasury Notes, Purchased in Connection with Forward Delivery Agreements (cont.)—GASB Statement No. 31 (GASB No. 31) states that investments in participating interest-earning investment contracts must be reported at fair value. The three forward delivery agreements with Wachovia Bank, NA (“Wachovia”) and one forward delivery agreement with Westdeutsche Landesbank Girozentral (“WestLB”) described in Note 4 would be considered participating investment contracts under GASB No. 31. Management has accounted for the agreements as investments in short-term U.S. treasury notes, at cost, rather than as investment contracts at fair value because management believes the difference between cost and fair value does not have a material impact on the financial statements. At June 30, 2005 and 2004, the fair value of the Fund’s interest in these three agreements exceeded the cost of the treasury securities owned by approximately \$2.8 million and \$1.0 million, respectively.

Investments—Investments that are stated at fair value include the State of Wisconsin Investment Board Local Government Investment Pool (see Note 3) and the State of Wisconsin General Obligation Clean Water Bonds (see Note 7). The Fund has received fair value information for investments from external sources. Changes in the fair value of investments are included in investment income. All other investments are reported at cost. Accrued interest on investments is recorded as earned. To the extent interest income on investments exceeds applicable arbitrage limits specified in the internal Revenue Code; the amount that must be rebated (“estimated arbitrage”) to the U.S. Treasury is recorded as a reduction of investment income (see Note 8). Investment transactions are recorded on the trade date.

Deferred Debt Expense—Issuance costs relating to the revenue obligation bonds are capitalized and are being amortized as a component of interest expense using the effective rate method.

Revenue Obligation Bonds—Interest expense on revenue obligation bonds is recognized on an accrual basis.

Debt Defeasance—Advance refundings of debt obligations that meet the criteria of GASB Statement No. 23 are recorded as an extinguishment of debt. The securities held in trust and the defeased obligations are not reported in the financial statements (see Note 6).

Deferred Charge—The Fund defers the difference between the reacquisition price and the net carrying amount of defeased debt and amortizes it as a component of interest expense over the shorter of the remaining life of the old debt or the life of the new debt. The unamortized deferred charge related to debt defeasance is classified as a reduction of revenue obligation bonds.

Cash Equivalents—The Fund considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. The Fund also considers as cash equivalents guaranteed investment contracts or repurchase agreements permitting withdrawals required by the bond resolution to meet insufficiencies in debt service payments. Repurchase agreements and guaranteed investment contracts are valued at cost because they are nonparticipating contracts due to the non-negotiability of these investments and because the amount of any withdrawals made do not consider market interest rates.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

Cash Equivalents (cont.)—Cash and cash equivalents in the Direct Loan Portfolio and Leveraged Loan Portfolio, while classified as unrestricted assets under accounting principles generally accepted in the United States (“GAAP”), are restricted as to use under federal statute and code and under the Clean Water Revenue Bond covenants and indenture. Those federal restrictions require that, with few exceptions, the funds can only be used for purposes of making loans to municipalities for program purposes, and that the funds must be kept available “in perpetuity” for such purposes. Likewise, the Clean Water Revenue Bond indenture specifies the use of bond proceeds, proceeds from loan repayments, and money in other accounts created under the bond indenture.

Net Assets—Net assets are classified as either restricted or unrestricted based on the presence or absence of restrictions.

Revenue Recognition—Loan interest and investment income are recognized as revenue when earned. Operating grants are recognized as revenue in the period the related expenditure occurs and include \$61.7 million and \$92.6 million of EPA contributions in 2005 and 2004, respectively.

Hardship Grants—Hardship grants are recognized as an expense when the funds are granted and disbursed.

Transfers In—Transfers in consist of capital contributions from the State of Wisconsin and are recognized as the contributions are received.

Estimates—The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NOTE 2 – LOANS TO LOCAL GOVERNMENTS

Loans to local governments at June 30, 2005 and 2004, represent loans for wastewater treatment projects or drinking water projects and are for terms of up to 20 years. These loans are made at a variety of prescribed interest rates based on project type categories. In order to effectuate statutory policy, virtually all of the loans issued by the Clean Water Fund Program, Safe Drinking Water Loan Program and Land Recycling Loan Program are at interest rates that are below the State’s cost of borrowing. The net losses that can result from this negative interest margin are funded by State transfers. Interest rates on loans receivable ranged from 0% to 5.8% in both 2005 and 2004. The weighted average interest rate was 2.999% and 2.94% at June 30, 2005 and 2004, respectively. The loans contractually are revenue obligations or general obligations of the local governments, or both. Additionally, various statutory provisions exist which provide further security for payment. In the event of a default, the State can intercept State aid payments due to the applicable local government, induce an additional charge to the amount of property taxes levied by the county in which the applicable local government is located, or both. Accordingly, no reserve for loan loss is deemed necessary. At June 30, 2005, all loans were performing in accordance with the contractual terms.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 2 – LOANS TO LOCAL GOVERNMENTS (cont.)

Of the loans outstanding at June 30, 2005 and 2004, \$408,701,660 and \$350,509,979 (29% and 27%), respectively, were loans due from the Milwaukee Metropolitan Sewerage District.

The Clean Water Fund Program, Safe Drinking Water Loan Program and Land Recycling Loan Program have made additional financial assistance commitments of \$152,192,733 as of June 30, 2005. From July 1, 2005 to October 6, 2005, the Fund made loan disbursements of \$30,055,437 from these additional commitments. These loan commitments are generally met through the proceeds from additional Federal grants and from the issuance of additional revenue obligation bonds (See Note 5).

NOTE 3 – CASH AND CASH EQUIVALENTS

As of June 30, 2005 and 2004, cash and cash equivalents consisted of the following:

	2005	2004
State of Wisconsin Investment Board (“SWIB”) Local Government Investment Pool (“LGIP”), at fair value	\$ 227,965,378	\$ 304,028,621
Investments reported at cost:		
MBIA Guaranteed Investment Agreement	6,250,292	6,250,292
Repurchase Agreement with Bayerische Landesbank	7,597,910	7,597,910
American International Group Matched Funding Corp. (“AIG”) Guaranteed Investment Agreement	21,842,081	21,842,081
Miscellaneous cash	488	-
	263,656,149	339,718,904
Less Amounts classified as restricted assets (see Note 5)	(72,700,346)	(68,576,666)
Total Unrestricted Cash and Cash Equivalents	\$ 190,955,803	\$ 271,142,238

The LGIP is an investment fund managed by SWIB that accepts investment deposits from over 1,000 municipalities and other public entities in the State of Wisconsin. The objectives of the LGIP are to provide safety of principal, liquidity, and a reasonable rate of return. The LGIP is insured as to credit risk. The LGIP functions in a manner similar to a money market fund in that the yield earned changes daily and participants may invest or withdraw any or all amounts on a daily basis at par value. The LGIP is strategically managed with a longer average life than a money market fund. The LGIP is not a Securities and Exchange Commission (“SEC”) registered investment, but is regulated by Wisconsin Statutes 25.14 and 25.17. At June 30, 2005, the current yield on the LGIP was 2.97%. The LGIP investment is stated at fair value.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 3 – CASH AND CASH EQUIVALENTS (cont.)

The investment with MBIA Investment Management Corporation is secured by a financial guarantee insurance policy issued by the MBIA Insurance Corporation. At June 30, 2005, the investment had a market value of \$7,159,969 and was accruing interest at the rate of 6.2%. The investment with AIG is secured by a financial guarantee insurance policy issued by the parent of AIG, American International Group. At June 30, 2005, the agreement had a market value of \$26,576,267 and was accruing interest at the rate of 8.1%.

The repurchase agreement with Bayerische Landesbank is collateralized by U.S. Treasury notes, bonds and debentures. At June 30, 2005, the repurchase agreement had a market value of \$7,843,470. The collateral is held by Wells Fargo Bank pursuant to a custody agreement. The repurchase agreement contains a fixed yield of 6.5%. Both the repurchase agreement, along with the MBIA and AIG investment agreements, provide for liquidation of investments at par if and when required by the terms of the Clean Water Revenue Bond General Resolution.

	Amount	GASB 3 Category	Credit Risk	Interest Rate Risk	Interest Rate Highly Sensitive	Foreign Currency Rate
LGIP	\$ 227,965,378	N/A	Not rated	28 days weighted average maturity	N/A	N/A
MBIA-GIC	6,250,292	N/A	Aaa	6-1-13 final maturity	N/A	N/A
Repo BL (vs. veterans affairs)	7,597,910	Category 1	Not rated	6-15-28 final maturity	N/A	N/A
AIG-GIC	21,842,081	N/A	Aa2	6-1-11 final maturity	N/A	N/A
Treasury notes – Forward delivery	23,386,696	Category 1	N/A	See Note 4	N/A	N/A
GO Bonds-WI	145,895,768	Category 1	Aa-	5-1-24 final maturity	N/A	N/A
Miscellaneous cash	488	N/A	N/A	N/A	N/A	N/A

The EIF does not have an investment policy for custodial credit risk, credit risk, or interest rate risk.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 4 – FORWARD DELIVERY AGREEMENTS

The Fund has entered into four agreements for the future delivery and purchase of securities to be held as investments of the loan credit reserve fund of the Revenue Obligation Bonds (see Note 5). Three of the agreements are with Wachovia and one is with WestLB and each provides for the delivery to, and purchase by, the Fund, of securities with a maturity value equal to the purchase price plus earnings calculated at the rate of the agreements. The agreements were entered into in conjunction with the 1993 Series 1, 1997 Series 1, 1998 Series 1, and 1999 Series 1 Revenue Obligation Bonds.

Every six months during the term of the agreements, Wachovia and WestLB are required to deliver United States Treasury securities (“Treasury securities”) to the Fund for purchase. The Treasury securities are held as investments by the Fund. The price paid by the Fund for the Treasury securities is determined under the contract. That price is that which results in the predetermined annual earnings rate computed on the notional amount, taking into account the coupon interest on the delivered Treasury securities. The redemption value of the securities purchased for investment must equal at least the purchase price of the securities plus earnings calculated by multiplying the notional amount times the annual earnings rate as calculated for the term until the next bond payment date. The Wachovia agreements may be terminated at the option of the Fund and a payment between the parties will be made to compensate for the difference in present value of the earnings expected under each agreement and the earnings available on similar agreements at the time of the termination, Management has asserted that it does not anticipate terminating the agreements at a time when a payment would be required from the Fund to Wachovia. If the agreements were terminated at a time when a payment would be due to Wachovia, management has also asserted that it would be able to enter into similar agreements that would have consistent present values as the agreements are valued in relation to prevailing Treasury security rates. In addition, if the agreements are terminated in whole or in part due to the need to use funds at the maturity date for making a debt service payment on the bonds, then there is not a compensating payment made between the parties.

The agreement with WestLB was amended effective December 10, 2002 to modify the termination provision. Other than a default by any of the parties to the agreement, the agreement may only be terminated on the last scheduled bond payment date for the 1993 Series 1 bonds which is June 1, 2013.

By GASB Statement No. 3 definition, these securities are classified as category one investments. The par values, coupon rates, the cost and rate at which the Treasury Notes accrue interest in accordance with the Forward Delivery Agreements at June 30, 2005, are as follows:

	Par Value of Treasuries	Coupon Rate of Treasuries	Cost of Treasuries	Agreement Interest Rate	Agreement Maturity Date	Agreement Market Value
Series 1997-1 Agreement	\$ 7,116,000	2.0%	\$ 6,992,011	5.58%	June 1, 2017	\$ 7,773,026
Series 1998-1 Agreement	7,401,000	2.0	7,292,215	5.01	June 1, 2018	7,754,590
Series 1993-1 Agreement	2,219,000	2.0	2,184,182	5.22	June 1, 2013	2,358,237
Series 1999-1 Agreement	7,066,000	2.0	6,918,023	6.32	June 1, 2020	8,376,140

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS

REVENUE OBLIGATION BONDS

Revenue bonds are payable only from revenues derived from the operation of the loan programs.

	Beginning Balance	Increases	Decreases	Ending Balance
Revenue bonds				
Add/(subtract) deferred amounts for:	\$ 682,935,000	\$ 107,025,000	\$ 148,525,000 *	\$ 641,435,000
Refundings-gains/(losses)	(9,924,692)	(7,275,553)	(2,623,862)	(14,576,383)
Premiums/discounts	19,101,139	11,408,668	5,155,647	25,354,160
 Totals	 \$ 692,111,447	 \$ 111,158,115	 \$ 151,056,785	 \$ 652,212,777

* - Includes \$109,185,000 of refunded bonds.

Revenue obligation serial and term bonds as of June 30, 2005 and 2004, consisted of the following:

	2005	2004
1991 Series 1:		
Term Bonds, mandatory redemption of bonds at 100% of par, June 1, 2009 through June 1, 2011	\$ 57,445,000	\$ 57,445,000
Unamortized discount on bonds	(134,357)	(156,575)
	57,310,643	57,288,425
 1993 Series 2:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2004	30,780,000	45,035,000
Unamortized premium on bonds	403,634	662,675
	31,183,634	45,697,675
 1995 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2006	-	4,365,000
Unamortized premium on bonds	-	44,158
	-	4,409,158
 1997 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2008	7,470,000	10,915,000
Unamortized premium on bonds	98,740	177,246
	7,568,740	11,092,246
 1998 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2008	31,385,000	65,780,000
Unamortized discount bonds	(95,680)	(28,543)
	31,289,320	65,751,457

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS (cont.)

	2005	2004
1998 Series 2:		
Serial Bonds, no optional redemption	\$ 90,400,000	\$ 90,400,000
Unamortized premium on bonds	4,167,567	4,668,245
	94,567,567	95,068,245
1999 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2009	13,220,000	50,740,000
Unamortized (discount) premium on bonds	29,999	(101,555)
	13,249,999	50,638,445
2001 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2011	41,535,000	62,825,000
Unamortized (discount) premium on bonds	(85,601)	554,754
	41,449,399	63,379,754
2002 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2012	65,980,000	94,295,000
Unamortized premium on bonds	359,976	1,580,395
	66,339,976	95,875,395
2002 Series 2:		
Serial Bonds, no optional redemption	79,400,000	84,340,000
Unamortized premium on bonds	4,193,103	5,293,402
	83,593,103	89,633,402
2004 Series 1:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2014	116,795,000	116,795,000
Unamortized premium on bonds	5,473,607	6,406,937
	122,268,607	123,201,937
2004 Series 2:		
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2015	107,025,000	-
Unamortized premium on bonds	10,943,172	-
	117,968,172	-
Total of All Series	666,789,160	702,036,139
Unamortized deferred charge related to debt defeasance (Note 6)	(14,576,383)	(9,924,692)
Revenue Obligation Bonds, Net of Deferred Charge	\$ 652,212,777	\$ 692,111,447

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS (cont.)

The original issue discount or premium at issuance and the interest rates at June 30, 2005, on the following bond series were:

Series	Original Issue Discount/ (Premium)	Interest Rates
1991 Series 1	\$ 1,366,407	6.875%
1993 Series 2	(2,349,253)	4.75 – 6.125%
1995 Series 1	(1,253,936)	6.25%
1997 Series 1	(288,312)	5.25 – 6.00%
1998 Series 1	(811,362)	4.00 – 5.00%
1998 Series 2	(7,739,808)	4.00 – 5.50%
1999 Series 1	(58,061)	5.00 – 5.75%
2001 Series 1	(1,022,362)	4.50 – 5.25%
2002 Series 1	(2,426,001)	4.00 – 5.25%
2002 Series 2	(7,344,300)	3.00 – 5.50%
2004 Series 1	(6,632,300)	4.00 – 5.00%
2004 Series 2	(11,408,668)	3.25 – 5.25%

Principal maturities of the bonds, net of advance refundings, as of June 30, 2005, are as follows:

Years Ending June 30,	Principal	Interest	Totals
2006	\$ 44,775,000	\$ 33,301,015	\$ 78,076,015
2007	47,085,000	30,906,521	77,991,521
2008	49,540,000	28,405,521	77,945,521
2009	52,020,000	26,111,359	78,131,359
2010	54,760,000	23,230,234	77,990,234
2011-2015	199,790,000	76,586,719	276,376,719
2016-2020	138,080,000	32,757,343	170,837,343
2021-2024	55,385,000	5,902,460	61,287,460
Totals	\$ 641,435,000	\$ 257,201,172	\$ 898,636,172

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS (cont.)

The revenue obligation bonds are collateralized by a security interest in all assets of the Leveraged Loan Portfolio. At June 30, 2005 and 2004, the total assets of the Leveraged Loan Portfolio were \$826,969,052 and \$868,903,622, respectively. Neither the full faith and credit nor the taxing power of the State is pledged for the payment of the revenue obligation bonds. However, as the loans granted to the municipalities are at an interest rate which is less than the Revenue Bond rate, the State is obligated by the Clean Water Fund General Resolution to fund, prior to each loan disbursement, a reserve, which subsidizes the Leveraged Loan Portfolio in an amount to offset this interest rate disparity.

Among other restrictions under the revenue obligation bond agreements are provisions that require that a specified amount of cash and investments be held by an independent trustee in a reserve account for the purpose of paying bond interest and principal when due. The restricted assets on the balance sheets consist of substantially all of the MBIA, AIG, Bayerische Landesbank investments (Note 3) and \$15 million of the LGIP balance held as a credit reserve. These amounts are required in order to satisfy the conditions of certain agreements related to maintaining the minimum credit ratings on the bonds.

NOTE 6 – ADVANCE REFUNDING

In 1993, the Fund defeased a portion of its 1991 Series 1 bonds through the issuance of 1993 Series 2 Refunding Bonds. The proceeds from the 1993 Series 2 Refunding Bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 30, 2005 and June 30, 2004 there was \$47,110,000 and \$60,865,000, respectively, of the defeased bonds outstanding that will be serviced by the irrevocable trust's remaining funds.

In 1998, the Fund defeased a portion of its 1991 Series 1, 1993 Series 1, 1995 Series 1 and 1997 Series 1 bonds through the issuance of \$104,360,000 of 1998 Series 2 Refunding Bonds. The proceeds from the 1998 Series 2 Refunding Bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 30, 2005, and 2004, there was \$91,985,000 of the defeased bonds outstanding that will be serviced by the irrevocable trust's remaining funds.

In 2002, the Fund defeased a portion of its 1993 Series 1, 1995 Series 1, 1997 Series 1, 1998 Series 1, and 1999 Series 1 bonds through the issuance of \$85,575,000 of 2002 Series 2 Refunding Bonds. The proceeds from the 2002 Series 2 Refunding Bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 30, 2005 and 2004, there was \$81,405,000 and \$86,095,000, respectively, of the defeased bonds outstanding that will be serviced by the irrevocable trust's remaining funds.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 6 – ADVANCE REFUNDING (cont.)

On January 25, 2005, the Fund issued \$107,025,000 in revenue bonds with an average interest rate of 5.11 percent to advance refund \$109,185,000 of its 1998 Series 1, 1999 Series 1, 2001 Series 1, and 2002 Series 1 bonds with an average interest rate of 5.24 percent. The net proceeds of \$117,380,148 (after payment of \$1,048,855 in underwriting fees, insurance and other issuance costs) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the refunded bonds. As a result, this portion of the bonds are considered to be defeased and the liability for those bonds has been removed from these financial statements.

The cash flow requirements on the refunded bonds and notes prior to the advance refunding was \$166,111,690 from 2005 through 2020. The cash flow requirements on the 2005 refunding bonds are \$160,718,638 from 2005 through 2020. The advance refunding resulted in an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$4,251,744.

NOTE 7 – TRANSFERS IN

Transfers in consist of contributions from the State of Wisconsin, net of amounts returned to the State of Wisconsin (all of which are statutorily mandated). Fiscal 2005 did not require any transfers in, but, rather, returned \$6,000,000 of capital to the state. Fiscal 2004 transfers in consist of \$38,320,000 of contributions offset by \$6,000,000 returned to the State of Wisconsin. The statutorily mandated return of capital is based on amounts the State general fund requires for debt service payments on obligations the State incurred to fund certain operating transfers to the Fund.

In April 2004, all of the State of Wisconsin General Obligation Bonds previously owned by the Fund were exchanged for \$116,840,689 (par value) of State of Wisconsin General Obligation Bond, Clean Water Fund Program ("Global Certificate"). The estimated market value and weighted average coupon interest rate of the Global Certificate at June 30, 2005 and 2004 is \$145,895,768 and 6.82% and \$135,016,318 and 6.1%, respectively. The Bonds are registered in the name of the Fund and held by an independent trustee.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 7 – TRANSFERS IN (cont.)

Principal maturities of the Global Certificate as of June 30 are as follows:

Years Ending June 30,	2005	2004
2006	\$ -	\$ -
2007	-	-
2008	-	-
2009	-	9,506,708
2010	14,518,075	16,480,847
2011-2015	45,467,534	40,371,006
2016-2020	36,726,010	32,609,343
2021-2024	20,129,070	17,872,785
Total	\$ 116,840,689	\$ 116,840,689

NOTE 8 – INVESTMENT INCOME

Investment income is recorded net of estimated required arbitrage relating to outstanding State of Wisconsin Clean Water Revenue Bonds and consisted of the following for the fiscal years ended June 30, 2005 and 2004:

	2005	2004
Interest:		
State of Wisconsin Investment Board Local Government Investment Pool	\$ 5,869,515	\$ 2,385,215
MBIA Guaranteed Investment Agreement	387,518	387,518
Repurchase Agreement with Bayerische Landesbank	493,864	493,864
AIG Guaranteed Investment Agreement	1,769,209	1,769,209
United States Treasury Notes	1,307,178	1,307,172
State of Wisconsin General Obligation Bonds	-	7,939,971
Total Interest	9,827,284	14,282,949
Changes in Unrealized Gains (Losses):		
State of Wisconsin Investment Board Local Government Investment Pool	(328,530)	49,091
State of Wisconsin General Obligation Bonds	10,879,450	(9,394,793)
Total Changes in Unrealized Gains (Losses)	10,550,920	(9,345,702)
Total Interest and Changes in Unrealized Gains (Losses)	20,378,204	4,937,247
Change in Estimated Rebtable Arbitrage Liability	(59,590)	447,299
TOTAL INVESTMENT INCOME	\$ 20,318,614	\$ 5,384,546

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 9 – TRANSACTIONS WITH RELATED PARTIES

The DNR and DOA have statutory duties to manage the Fund. Expenses relating to the management of the Fund are allocated to and paid by the Fund. Total allocated expenses from DNR and DOA, which are reflected in the statement of revenues, expenses and changes in fund equity for the years ended June 30, 2005 and 2004 were \$4,295,580 and \$5,841,297, respectively. The Fund allocates DNR and DOA expenses to the Direct Loan Portfolio, the Proprietary Loan/Grant Portfolio, the Drinking Water Loan Portfolio and the Leveraged Loan Portfolio.

The following details total salaries and benefits by agency for the fiscal years ended June 30, 2005 and 2004:

	<u>2005</u>	<u>2004</u>
DNR	\$ 3,015,374	\$ 4,451,092
DOA	<u>582,633</u>	<u>565,172</u>
Total	<u>\$ 3,598,007</u>	<u>\$ 5,016,264</u>

NOTE 10 – OPERATING GRANTS AND HARDSHIP GRANTS

EPA Operating Grants for Wastewater Projects—The Federal Water Quality Act of 1987 (the “Water Quality Act”) established a joint Federal and state program with the EPA to assist in providing financial assistance to municipalities within the states for governmentally owned wastewater treatment projects. Under the terms of the EPA grant, the State was required (1) to establish the Clean Water Fund Program, a perpetual state revolving fund into which the grant monies must be deposited, (2) to provide State matching funds equal to 20% of the grant and (3) to use the monies to provide financial assistance to municipalities for governmental owned wastewater treatment projects in a number of ways, provided that such assistance is not in the form of a grant. Reauthorization of the Water Quality Act of 1987 is expected to result in the allocation of capitalization grant to Wisconsin of approximately \$29.1 million for federal fiscal year 2005. Four percent of the EPA grant amount may be used for wastewater program administrative expenses. Authorization levels for years after 2005 are unknown at this time.

EPA Operating Grants for Drinking Water Projects—The Federal Safe Drinking Water Act Amendment of 1996 (the “Safe Drinking Water Act”) established a joint Federal and State program with the EPA to assist in providing financial assistance to municipal and community water system projects. Under the terms of the EPA grant, the State was required (1) to establish the Safe Drinking Water Loan Program, a perpetual state revolving fund into which the grant monies must be deposited, (2) to provide State matching funds equal to 20% of the grant and (3) to use the monies to provide financial assistance to municipal and community water system projects. The Safe Drinking Water Act was authorized through federal fiscal year 2005 and a grant to Wisconsin of approximately \$16.4 million is expected for federal fiscal year 2005.

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

NOTES TO FINANCIAL STATEMENTS Years Ended June 30, 2005 and 2004

NOTE 10 – OPERATING GRANTS AND HARDSHIP GRANTS (cont.)

Reauthorization of the Safe Drinking Water Act may not be acted upon by the present Congress of the United States, although the Fund expects EPA capitalization grants to states to continue into the future. Four percent of the EPA grant amount may be used for water program administrative expenses plus a portion of the grant may be used by DNR for various water-related issues and initiatives.

Hardship Grants—Wisconsin statutes require that the Fund provide financial hardship assistance for wastewater projects to communities that qualify under Wisconsin Statute 281.58(13). This assistance may come in the form of reduced interest rates (as low as 0%) or grants subject to limitations prescribed by the statute. In 2005 and 2004, the Fund expended hardship grants of \$858,753 and \$1,065,392, respectively. At June 30, 2004, the Fund was not committed to award any additional hardship grants. At June 30, 2005, the Fund had committed to award \$4,260,441 of additional hardship grants.

S U P P L E M E N T A L I N F O R M A T I O N

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENT OF NET ASSETS
BY PROGRAM
June 30, 2005

ASSETS	Clean Water Fund Program		
	Direct Loan Portfolio	Proprietary Portfolio	Leveraged Loan Portfolio
Current Assets			
Unrestricted cash and cash equivalents	\$ 114,910,893	\$ 11,271,980	\$ 9,790,598
United States Treasury Notes, purchased in connection with forward delivery agreements, at cost	-	-	23,386,696
Receivables			
Loans to local governments - current portion	48,469,022	1,592,830	43,538,338
Due from other funds	-	2,423,836	-
Due from other governmental entities	4,183,158	78,042	2,786,502
Accrued investment income	-	-	329,808
Prepaid items	-	4,060	16,887
Total Current Assets	<u>167,563,073</u>	<u>15,370,748</u>	<u>79,848,829</u>
Noncurrent Assets			
Restricted assets - cash equivalents	-	-	72,700,346
Investments - State of Wisconsin general obligation clean water bonds, at fair value	-	-	145,895,768
Loans to local governments	647,403,247	18,316,480	525,394,642
Prepaid items	-	-	302,558
Deferred debt expense	-	-	2,826,909
Total Noncurrent Assets	<u>647,403,247</u>	<u>18,316,480</u>	<u>747,120,223</u>
TOTAL ASSETS	<u>\$ 814,966,320</u>	<u>\$ 33,687,228</u>	<u>\$ 826,969,052</u>

Safe Drinking Water Loan Program	Eliminations	Totals
\$ 54,982,332	\$ -	\$ 190,955,803
-	-	23,386,696
6,229,630	-	99,829,820
-	(2,221,634)	202,202
752,225	-	7,799,927
-	-	329,808
-	-	20,947
<u>61,964,187</u>	<u>(2,221,634)</u>	<u>322,525,203</u>
-	-	72,700,346
-	-	145,895,768
109,766,759	-	1,300,881,128
-	-	302,558
-	-	2,826,909
<u>109,766,759</u>	<u>-</u>	<u>1,522,606,709</u>
<u>\$ 171,730,946</u>	<u>\$ (2,221,634)</u>	<u>\$ 1,845,131,912</u>

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENT OF NET ASSETS
BY PROGRAM
June 30, 2005

	Clean Water Fund Program		
	Direct Loan Portfolio	Proprietary Portfolio	Leveraged Loan Portfolio
<i>LIABILITIES AND NET ASSETS</i>			
Current Liabilities			
Accrued expenses	\$ 22,952	\$ 74,355	\$ -
Accrued interest on bonds	-	-	2,775,085
Due to other funds	156,115	1,682,060	2,221,634
Due to other governmental entities	-	-	472,844
Revenue obligation bonds - current maturities	-	-	44,775,000
Total Current Liabilities	<u>179,067</u>	<u>1,756,415</u>	<u>50,244,563</u>
Noncurrent Liabilities			
Revenue obligation bonds, net (including deferred charge)	-	-	607,437,777
Due to other governmental entities	-	-	996,824
Accrued expenses	-	30,832	-
Total Noncurrent Liabilities	<u>-</u>	<u>30,832</u>	<u>608,434,601</u>
Total Liabilities	<u>179,067</u>	<u>1,787,247</u>	<u>658,679,164</u>
Net Assets			
Restricted for environmental improvement	814,787,253	2,047,483	168,289,888
Unrestricted	-	29,852,498	-
Total Net Assets	<u>814,787,253</u>	<u>31,899,981</u>	<u>168,289,888</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 814,966,320</u>	<u>\$ 33,687,228</u>	<u>\$ 826,969,052</u>

Safe Drinking Water Loan Program		
	Eliminations	Totals
\$ 94,809	\$ -	\$ 192,116
-	-	2,775,085
47,680	(2,221,634)	1,885,855
-	-	472,844
-	-	44,775,000
<u>142,489</u>	<u>(2,221,634)</u>	<u>50,100,900</u>
-	-	607,437,777
-	-	996,824
-	-	30,832
-	-	608,465,433
<u>142,489</u>	<u>(2,221,634)</u>	<u>658,566,333</u>
171,588,457	-	1,156,713,081
-	-	29,852,498
<u>171,588,457</u>	<u>-</u>	<u>1,186,565,579</u>
<u>\$171,730,946</u>	<u>\$ (2,221,634)</u>	<u>\$ 1,845,131,912</u>

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
BY PROGRAM
For the Year Ended June 30, 2005

	Clean Water Fund Program		
	Direct Loan Portfolio	Proprietary Portfolio	Leveraged Loan Portfolio
OPERATING REVENUES			
Loan interest	\$ 19,323,743	\$ 493,367	\$ -
Interest income used as security for revenue bonds	-	-	17,674,648
Other	-	46,550	217
Total Operating Revenues	<u>19,323,743</u>	<u>539,917</u>	<u>17,674,865</u>
OPERATING EXPENSES			
Interest	-	-	33,677,059
Salaries and benefits	552,389	429,949	1,719,791
Contractual services and other	44,257	125,462	572,169
Total Operating Expenses	<u>596,646</u>	<u>555,411</u>	<u>35,969,019</u>
Operating Income (Loss)	<u>18,727,097</u>	<u>(15,494)</u>	<u>(18,294,154)</u>
NONOPERATING REVENUES (EXPENSES)			
Investment income	2,650,442	137,435	-
Investment income used as security for revenue bonds	-	-	16,404,323
Operating grants	35,820,286	-	-
Hardship grants awarded	-	(858,753)	-
Total Nonoperating Revenues, Net	<u>38,470,728</u>	<u>(721,318)</u>	<u>16,404,323</u>
INCOME BEFORE TRANSFERS	57,197,825	(736,812)	(1,889,831)
Transfers in/(out)	<u>1,346,709</u>	<u>(7,413,041)</u>	<u>-</u>
Increase (Decrease) in Net Assets	58,544,534	(8,149,853)	(1,889,831)
TOTAL NET ASSETS - Beginning of Year	<u>756,242,719</u>	<u>40,049,834</u>	<u>170,179,719</u>
TOTAL NET ASSETS - END OF YEAR	<u>\$ 814,787,253</u>	<u>\$ 31,899,981</u>	<u>\$ 168,289,888</u>

Safe Drinking Water Loan Program	Eliminations	Totals
\$ 2,667,882	\$ -	\$ 22,484,992
-	-	17,674,648
-	-	46,767
<u>2,667,882</u>	-	<u>40,206,407</u>
-	-	33,677,059
895,878	-	3,598,007
606,641	-	1,348,529
<u>1,502,519</u>	-	<u>38,623,595</u>
<u>1,165,363</u>	-	<u>1,582,812</u>
1,126,414	-	3,914,291
-	-	16,404,323
25,893,067	-	61,713,353
-	-	(858,753)
<u>27,019,481</u>	-	<u>81,173,214</u>
28,184,844	-	82,756,026
-	-	(6,066,332)
28,184,844	-	76,689,694
<u>143,403,613</u>	-	<u>1,109,875,885</u>
<u>\$ 171,588,457</u>	<u>\$ -</u>	<u>\$ 1,186,565,579</u>

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENT OF CASH FLOWS
BY PROGRAM
For the Year Ended June 30, 2005

	Clean Water Fund Program		
	Direct Loan Portfolio	Proprietary Portfolio	Leveraged Loan Portfolio
CASH FLOWS FROM OPERATING ACTIVITIES			
Payments to employees for services	\$ (888,200)	\$ 158,538	\$ (1,546,038)
Payments to suppliers and other	(39,253)	64,354	(1,023,534)
Other operating revenues (expenses)	-	46,550	217
Net Cash Flows From (used by) Operating Activities	<u>(927,453)</u>	<u>269,442</u>	<u>(2,569,355)</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES			
Operating grants received	36,242,273	-	-
Grants paid	-	(858,753)	-
Transfers in (out)	1,346,709	(7,413,041)	-
Proceeds from issuance of long-term debt	-	-	117,509,813
Refunding bond proceeds deposited in irrevocable trust	-	-	(117,380,148)
Retirement of long-term debt	-	-	(39,340,000)
Interest payments	-	-	(34,573,762)
Net Cash Flows From Noncapital Financing Activities	<u>37,588,982</u>	<u>(8,271,794)</u>	<u>(73,784,097)</u>
CASH FLOWS FROM INVESTING ACTIVITIES			
Origination of loans	(110,612,270)	(1,796,655)	(51,008,450)
Collection on loans	40,443,088	1,587,453	41,187,752
Interest received on loans	19,159,170	486,690	17,604,659
Purchase of investments	-	-	(46,773,506)
Liquidation of investments	-	-	46,773,242
Increase in restricted cash equivalents	-	-	(4,123,680)
Investment and interest income	2,650,440	137,435	5,368,610
Net Cash Flows From Investing Activities	<u>(48,359,572)</u>	<u>414,923</u>	<u>9,028,627</u>
Net Increase (Decrease) in Unrestricted Cash and Cash Equivalents	(11,698,043)	(7,587,429)	(67,324,825)
CASH AND CASH EQUIVALENTS - Beginning of Year	<u>126,608,936</u>	<u>18,859,409</u>	<u>77,115,423</u>
CASH AND CASH EQUIVALENTS - END OF YEAR	<u>\$114,910,893</u>	<u>\$ 11,271,980</u>	<u>\$ 9,790,598</u>

Safe Drinking Water Loan Program	Eliminations	Totals
\$ (926,525)	\$ -	\$ (3,202,225)
(693,029)	-	(1,691,462)
-	-	46,767
<u>(1,619,554)</u>	<u>-</u>	<u>(4,846,920)</u>
26,247,719	-	62,489,992
-	-	(858,753)
-	-	(6,066,332)
-	-	117,509,813
-	-	(117,380,148)
-	-	(39,340,000)
-	-	(34,573,762)
<u>26,247,719</u>	<u>-</u>	<u>(18,219,190)</u>
(27,328,618)	-	(190,745,993)
5,402,722	-	88,621,015
2,595,179	-	39,845,698
-	-	(46,773,506)
-	-	46,773,242
-	-	(4,123,680)
<u>1,126,414</u>	<u>-</u>	<u>9,282,899</u>
<u>(18,204,303)</u>	<u>-</u>	<u>(57,120,325)</u>
6,423,862	-	(80,186,435)
<u>48,558,470</u>	<u>-</u>	<u>271,142,238</u>
<u>\$ 54,982,332</u>	<u>\$ -</u>	<u>\$ 190,955,803</u>

**STATE OF WISCONSIN
ENVIRONMENTAL IMPROVEMENT FUND**

STATEMENT OF CASH FLOWS
BY PROGRAM
For the Year Ended June 30, 2005

	Clean Water Fund Program		
	Direct Loan Portfolio	Proprietary Portfolio	Leveraged Loan Portfolio
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH FLOWS FROM OPERATING ACTIVITIES			
Operating income (Loss)	\$ 18,727,097	\$ (15,494)	\$ (18,294,154)
ADJUSTMENTS TO RECONCILE OPERATING INCOME (LOSS) TO NET CASH FLOWS FROM OPERATING ACTIVITIES			
Amortization	-	-	(647,200)
Interest income classified as investing activity	(19,323,743)	(493,367)	(17,674,648)
Interest expense classified as noncapital financing activity	-	-	34,507,280
Changes in assets and liabilities:			
Prepaid items	-	(78)	(319,445)
Deferred debt expense	-	-	(151,380)
Due from other funds	-	(120,426)	-
Accrued expenses	5,995	(2,232)	-
Accrued interest on bonds	-	-	(183,021)
Due to other funds	(336,802)	901,039	193,213
Due to other governmental entities	-	-	-
Total Adjustments	(19,654,550)	284,936	15,724,799
NET CASH USED IN OPERATIONS	\$ (927,453)	\$ 269,442	\$ (2,569,355)

Safe Drinking Water Loan Program	Eliminations	Totals
<u>\$ 1,165,363</u>	<u>\$ -</u>	<u>\$ 1,582,812</u>
-	-	(647,200)
(2,667,882)	-	(40,159,640)
-	-	34,507,280
-	-	(319,523)
-	-	(151,380)
-	193,213	72,787
(52,224)	-	(48,461)
-	-	(183,021)
(33,491)	(193,213)	530,746
(31,320)	-	(31,320)
<u>(2,784,917)</u>	<u>-</u>	<u>(6,429,732)</u>
<u>\$ (1,619,554)</u>	<u>\$ -</u>	<u>\$ (4,846,920)</u>

STATE OF WISCONSIN ENVIRONMENTAL IMPROVEMENT FUND

OTHER INFORMATION (UNAUDITED)
Years Ended June 30, 2005 and 2004

In management's opinion, the Governmental Accounting Standards Board (GASB) does not require an MD&A for individual fund reports under GASB Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. Therefore, the State has not prepared an MD&A for the State of Wisconsin Environmental Improvement Fund. An MD&A is included in the Comprehensive Annual Financial Report for the State of Wisconsin, which includes all funds and component units.

STATE OF WISCONSIN
LEVERAGED LOAN PORTFOLIO
FINANCIAL STATEMENTS
For the Year Ended June 1, 2005 and
Independent Auditors' Report



INDEPENDENT AUDITORS' REPORT

To the Secretary of the Department of Administration
and the Secretary of the Department of
Natural Resources of the State of Wisconsin

We have audited the accompanying financial statements of the Leveraged Loan Portfolio (an environmental financing program) of the State of Wisconsin Environmental Improvement Fund (an enterprise fund of the State of Wisconsin), as of June 1, 2005, and for the year then ended as listed in the table of contents. These financial statements are the responsibility of management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

As discussed in Note 1, the financial statements present only the Leveraged Loan Portfolio of the State of Wisconsin Environmental Improvement Fund and are not intended to present fairly the financial position of the State of Wisconsin, and the changes in its financial position and its cash flows in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Leveraged Loan Portfolio of the State of Wisconsin Environmental Improvement Fund as of June 1, 2005, and the changes in its financial position and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The Leveraged Loan Portfolio of the State of Wisconsin Environmental Improvement Fund has not presented the management's discussion and analysis that accounting principles generally accepted in the United States of America require to supplement, although not to be part of, the financial statements.

The "Other Information" on page 49 is presented for informational purposes only and is not a required part of the financial statements of the Leveraged Loan Portfolio of the State of Wisconsin Environmental Improvement Fund. The information has not been audited by us, and, accordingly, we express no opinion on such information.

Madison, Wisconsin
October 6, 2005

A handwritten signature in black ink that reads "Virchow Krause & Company LLP". The signature is written in a cursive, flowing style.

Page 33

**STATE OF WISCONSIN
LEVERAGED LOAN PORTFOLIO**

STATEMENT OF NET ASSETS
June 1, 2005

ASSETS	
Current Assets	
Unrestricted cash and cash equivalents	\$ 12,241,191
United States Treasury Notes, purchased in connection with forward delivery agreements, at cost	23,386,696
Receivables	
Loans to local governments - current portion	43,456,140
Due from other governmental entities	1,416,866
Prepaid items	16,887
Total Current Assets	<u>80,517,780</u>
Noncurrent Assets	
Restricted assets - cash equivalents	72,506,726
Investments - State of Wisconsin general obligation clean water bonds, at fair value	145,944,883
Loans to local governments	523,101,253
Prepaid items	303,965
Deferred debt expense	2,868,494
Total Noncurrent Assets	<u>744,725,321</u>
TOTAL ASSETS	<u>\$ 825,243,101</u>
LIABILITIES AND NET ASSETS	
Current Liabilities	
Due to other funds	\$ 2,036,497
Due to other governmental entities	472,844
Revenue obligation bonds - current maturities	44,775,000
Total Current Liabilities	<u>47,284,341</u>
Noncurrent Liabilities	
Due to other governmental entities	964,827
Revenue obligation bonds, net (including deferred charge)	607,554,178
Total Noncurrent Liabilities	<u>608,519,005</u>
Total Liabilities	<u>655,803,346</u>
Net Assets	
Restricted for environmental improvement	169,439,755
Total Net Assets	<u>169,439,755</u>
TOTAL LIABILITIES AND NET ASSETS	<u>\$ 825,243,101</u>

See accompanying notes to financial statements.

**STATE OF WISCONSIN
LEVERAGED LOAN PORTFOLIO**

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
For the Year Ended June 1, 2005

OPERATING REVENUES	
Interest income used as security for revenue bonds	\$ 17,640,247
OPERATING EXPENSES	
Interest	33,881,644
Salaries and benefits	1,705,311
Contractual services and other	<u>569,141</u>
Total Operating Expenses	<u>36,156,096</u>
Operating Loss	<u>(18,515,849)</u>
NONOPERATING REVENUES	
Investment income	4
Investment income used as security for revenue bonds	<u>17,917,908</u>
Total Nonoperating Revenues, Net	<u>17,917,912</u>
Decrease in Net Assets	(597,937)
TOTAL NET ASSETS - Beginning of Year	<u>170,037,692</u>
TOTAL NET ASSETS - END OF YEAR	<u>\$ 169,439,755</u>

See accompanying notes to financial statements.

**STATE OF WISCONSIN
LEVERAGED LOAN PORTFOLIO**

STATEMENT OF CASH FLOWS
For the Year Ended June 1, 2005

CASH FLOWS FROM OPERATING ACTIVITIES

Payments to employees for services	\$ (1,546,038)
Payments to suppliers and other	<u>(1,023,780)</u>
Net Cash Flows From Operating Activities	<u>(2,569,818)</u>

CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES

Proceeds from issuance of long-term debt	117,509,813
Refunding bond proceeds deposited in irrevocable trust	(117,380,148)
Retirement of long-term debt	(39,340,000)
Interest payments	<u>(34,573,762)</u>
Net Cash Flows From Noncapital Financing Activities	<u>(73,784,097)</u>

CASH FLOWS FROM INVESTING ACTIVITIES

Origination of loans	(50,245,980)
Collection on loans	41,187,752
Interest and dividends received	5,351,800
Purchase of investments	(46,773,506)
Liquidation of investments	46,773,243
Increase in restricted cash equivalents	(4,061,640)
Investment and interest income	<u>17,604,659</u>
Net Cash Flows From Investing Activities	<u>9,836,328</u>

Net Increase (decrease) in unrestricted cash and cash equivalents	(66,517,587)
--	--------------

CASH AND CASH EQUIVALENTS - Beginning of Year	<u>78,758,778</u>
---	-------------------

CASH AND CASH EQUIVALENTS - END OF YEAR	<u><u>\$ 12,241,191</u></u>
--	-----------------------------

**RECONCILIATION OF OPERATING LOSS TO NET CASH
USED IN OPERATION**

Operating Loss \$ (18,515,849)

**ADJUSTMENTS TO RECONCILE OPERATING LOSS TO NET
CASH USED IN OPERATION**

Amortization (692,119)

Interest income classified as investing activity (17,640,247)

Interest expense classified as noncapital financing activity 34,573,762

Changes in assets and liabilities:

Prepaid items (320,852)

Deferred debt expenses (151,625)

Due to other funds 177,112

Total Adjustments 15,946,031

NET CASH USED IN OPERATIONS \$ (2,569,818)

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity—The Leveraged Loan Portfolio (the “Portfolio”) is one of three portfolios of the Clean Water Fund Program, an environmental financing program of the State of Wisconsin Environmental Improvement Fund (the “Fund”). The Fund is an enterprise fund of the State of Wisconsin (the “State”) administered by the State of Wisconsin Department of Natural Resources (the “DNR”) and the State of Wisconsin Department of Administration (the “DOA”).

The Portfolio is funded by proceeds of revenue obligation bonds and contributions from the State. Assets in the Portfolio are used for loans for Wisconsin municipal wastewater projects that meet applicable State eligibility and reporting requirements.

The Fund applies all applicable Governmental Accounting Standards Board (“GASB”) pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

Net Operating Loss—The Portfolio incurred an operating loss of \$18.5 million in 2005. Management expects the Portfolio will generally incur net operating losses for the foreseeable future. As explained in Note 2, the losses result from the Portfolio’s statutory mission to provide loans to municipalities at interest rates below the Portfolio’s own cost of funds. The losses have historically been funded by transfers from the State. No transfers were required in 2005. Management expects transfers will continue for the foreseeable future sufficient to fund both the future operating losses and, together with additional borrowing, to fund additional loans to municipalities.

Interest on Loans Receivable—Interest on loans receivable is recognized on an accrual basis and recorded within Due From Other Governmental Entities on the statement of net assets.

United States Treasury Notes, Purchased in Connection with Forward Delivery Agreements—The Portfolio holds United States Treasury Notes as investments at June 1, 2005 and records the notes at cost. The Portfolio purchased these securities in accordance with the Forward Delivery Agreements (see Note 4).

GASB Statement No. 31 (GASB No. 31) states that investments in participating interest-earning investment contracts must be reported at fair value. The three forward delivery agreements with Wachovia Bank, NA (“Wachovia”) and one forward delivery agreement with Westdeutsche Landesbank Girozentral (“WestLB”) described in Note 4 would be considered participating investment contracts under GASB No. 31. Management has accounted for the agreements as investments in short-term U.S. treasury notes, at cost, rather than as investment contracts at fair value because management believes the difference between cost and fair value does not have a material impact on the financial statements. At June 1, 2005, the fair value of the Fund’s interest in these three agreements exceeded the cost of the treasury securities owned by approximately \$2.9 million.

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

Investments—Investments that are stated at fair value include the State of Wisconsin Investment Board (“SWIB”) Local Government Investment Pool (“LGIP”) (see Note 3). The Portfolio has received fair value information for investments from external sources. Changes in the fair value of investments are included in investment income. All other investments are reported at cost. Accrued interest on investments is recorded as earned. To the extent interest income on investments exceeds applicable arbitrage limits specified in the Internal Revenue Code, the amount that must be rebated (“estimated arbitrage”) to the U.S. Treasury is recorded as a reduction of investment income (see Note 8). Investment transactions are recorded on the trade date.

Deferred Debt Expense—Issuance costs relating to the revenue obligation bonds were capitalized and are being amortized as a component of interest expense using the effective rate method.

Revenue Obligation Bonds—Interest expense on revenue obligation bonds is recognized on an accrual basis.

Debt Defeasance—Advance refundings of debt obligations that meet the criteria of GASB Statement No. 23 are recorded as an extinguishment of debt. The securities held in trust and the defeased obligations are not reported in the financial statements (see Note 6).

Deferred Charge—The Portfolio defers the difference between the reacquisition price and the net carrying amount of defeased debt and amortizes it as a component of interest expense over the shorter of the remaining life of the old debt or the life of the new debt. The unamortized deferred charge related to debt defeasance is classified as a reduction of revenue obligation bonds.

Cash Equivalents—The Portfolio considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. The Portfolio also considers as cash equivalents guaranteed investment contracts or repurchase agreements permitting withdrawals required by the bond resolution to meet insufficiencies in debt service payments. Repurchase agreements and guaranteed investment contracts are valued at cost because they are nonparticipating contracts due to the non-negotiability of these investments and because the amount of any withdrawals made do not consider market interest rates.

Net Assets—Net assets are classified as either restricted or unrestricted based on the presence or absence of restrictions.

Transfers In—Transfers in consist of capital contributions from the State of Wisconsin and are recognized as the contributions are received.

Estimates—The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 1 – NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (cont.)

Future Accounting Pronouncement—In March 2003, the GASB issued Statement No. 40, *Deposit and Investment Risk Disclosures - an amendment of GASB Statement No. 3*. GASB Statement No. 40 is effective for fiscal periods beginning after June 15, 2004 and establishes and modifies disclosure requirements, related to investment and deposit risks (including credit risk, interest rate risk and foreign currency risk). The adoption of this statement in fiscal 2006 is not expected to have a material impact on the Fund's financial statements.

NOTE 2 – LOANS TO LOCAL GOVERNMENTS

Leveraged loans to local governments at June 1, 2005, represent loans for wastewater treatment projects and are for terms of up to 20 years. These loans are made at a variety of prescribed interest rates based on project type categories. In order to effectuate statutory policy, a majority of the loans issued by the Portfolio are at interest rates that are below the State's cost of borrowing. The net losses that can result from this negative interest margin are funded by State contributions. Interest rates on loans receivable ranged from 0% to 5.8% in 2004. The weighted average interest rate was 3.001% at June 1, 2005. The loans contractually are revenue obligations or general obligations of the local governments, or both. Additionally, various statutory provisions exist which provide further security for payment. In the event of a default, the State can intercept State aid payments due to the applicable local government, induce an additional charge to the amount of property taxes levied by the county in which the applicable local government is located, or both. Accordingly, no reserve for loan loss is deemed necessary.

Of the loans outstanding at June 1, 2005, \$389,473,928 (28%) were loans due from the Milwaukee Metropolitan Sewerage District.

The Portfolio has made additional financial assistance commitments of \$97,837,967 as of June 1, 2005. From June 1, 2005 to October 6, 2005, the Portfolio made loan disbursements of \$26,315,133 from these additional commitments. These loan commitments are generally met through the proceeds from additional Federal grants and from the issuance of additional revenue obligation bonds (see Note 5).

NOTE 3 – CASH AND CASH EQUIVALENTS

As of June 1, 2005, cash and cash equivalents consisted of the following:

Local Government Investment Pool ("LGIP"), at fair value	\$ 49,056,239
Cash held by trustee	1,395
Investments reported at cost:	
MBIA Guaranteed Investment Agreement	6,250,292
Repurchase Agreement with Bayerische Landesbank	7,597,910
American International Group Matched Funding Corp. (AIG) Guaranteed Investment Agreement	<u>21,842,081</u>
	84,747,917
Less: Amounts classified as restricted assets (see Note 5)	<u>(72,506,726)</u>
Total Unrestricted Cash and Cash Equivalents	<u>\$ 12,241,191</u>

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 3 – CASH AND CASH EQUIVALENTS (cont.)

The LGIP is an investment fund managed by SWIB that accepts investment deposits from over 1,000 municipalities and other public entities in the State of Wisconsin. The objectives of the LGIP are to provide safety of principal, liquidity, and a reasonable rate of return. The LGIP is insured as to credit risk. The LGIP functions in a manner similar to a money market fund in that the yield earned changes daily and participants may invest or withdraw any or all amounts on a daily basis at par value. The LGIP is strategically managed with a longer average life than a money market fund. The LGIP is not a SEC registered investment, but is regulated by Wisconsin Statutes 25.14 and 25.17. At June 1, 2005, the current yield on the LGIP was 2.89%. The LGIP investment is stated at fair value.

The investment with MBIA Investment Management Corporation is secured by a financial guarantee insurance policy issued by the MBIA Insurance Corporation. At June 1, 2005, the investment had a market value of \$7,192,533 and was accruing interest at the rate of 6.2%. The investment with AIG is secured by a financial guarantee insurance policy issued by the parent of AIG, American International Group. At June 1, 2005, the agreement had a market value of \$26,739,499 and was accruing interest at the rate of 8.1%.

The repurchase agreement with Bayerische Landesbank is collateralized by U.S. Treasury notes, bonds and debentures. At June 1, 2005, the repurchase agreement had a market value of \$9,091,177. The collateral is held by Wells Fargo Bank pursuant to a custody agreement. The repurchase agreement contains a fixed yield of 6.5%. Both the repurchase agreement, along with the MBIA and AIG investment agreements, provide for liquidation of investments at par if and when required by the terms of the Clean Water Revenue Bond General Resolution.

NOTE 4 – FORWARD DELIVERY AGREEMENTS

The Portfolio has entered into four agreements for the future delivery and purchase of securities to be held as investments of the loan credit reserve fund of the Revenue Obligation Bonds (see Note 5). Three of the agreements are with Wachovia and one is with WestLB and each provides for the delivery to, and purchase by, the Portfolio, of securities with a maturity value equal to the purchase price plus earnings calculated at the rate of the agreements. The agreements were entered into in conjunction with the 1993 Series 1, 1997 Series 1, 1998 Series 1, and 1999 Series 1 Revenue Obligation Bonds.

Every six months during the term of the agreements, Wachovia and WestLB are required to deliver United States Treasury securities ("Treasury securities") to the Portfolio for purchase. The Treasury securities are held as investments by the Portfolio. The price paid by the Portfolio for the Treasury securities is determined under the contract. That price is that which results in the predetermined annual earnings rate computed on the notional amount, taking into account the coupon interest on the delivered Treasury securities. The redemption value of the securities purchased for investment must equal at least the purchase price of the securities plus earnings calculated by multiplying the notional amount times the annual earnings rate as calculated for the term until the next bond payment date. The Wachovia agreements may be terminated at the option of the Portfolio and a payment between the parties will be made to compensate for the difference in present value of the earnings expected under each agreement and the earnings available on similar agreements at the time of the termination.

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 4 – FORWARD DELIVERY AGREEMENTS (cont.)

Management has asserted that it does not anticipate terminating the agreements at a time when a payment would be required from the Portfolio to Wachovia. If the agreements were terminated at a time when a payment would be due to Wachovia, management has also asserted that it would be able to enter into similar agreements that would have consistent present values as the agreements are valued in relation to prevailing Treasury security rates. In addition, if the agreements are terminated in whole or in part due to the need to use funds at the maturity date for making a debt service payment on the bonds, then there is not a compensating payment made between the parties.

The forward delivery agreement with WestLB was amended effective December 10, 2002 to modify the agreement termination provision. Other than a default by any of the parties to the agreement, the agreement may only be terminated on the last scheduled bond payment date for the 1993 Series 1 bonds which is June 1, 2013.

By GASB Statement No. 3 definition, these securities are classified as category one investments. The par values, coupon rates, the cost and rate at which the Treasury Notes accrue interest in accordance with the Forward Delivery Agreements at June 1, 2005, are as follows:

	Par Value of Treasuries	Coupon Rate of Treasuries	Cost of Treasuries	Agreement Interest Rate	Agreement Maturity Date	Agreement Market Value
Series 1997-1 Agreement	\$ 7,116,000	2.0%	\$ 6,992,011	5.58%	June 1, 2017	\$ 7,792,354
Series 1998-1 Agreement	7,401,000	2.0	7,292,215	5.01	June 1, 2018	7,770,282
Series 1993-1 Agreement	2,219,000	2.0	2,184,182	5.22	June 1, 2013	2,368,055
Series 1999-1 Agreement	7,066,000	2.0	6,918,023	6.32	June 1, 2020	8,390,704

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS

REVENUE OBLIGATION BONDS

Revenue bonds are payable only from revenues derived from the operation of the loan programs.

	Beginning Balance	Increases	Decreases	Ending Balance
Revenue bonds				
Add/(subtract) deferred amounts for:	\$ 682,935,000	\$ 107,025,000	\$ 148,525,000 *	\$ 641,435,000
Refundings-gains/(losses)	(10,115,254)	(7,275,553)	(2,581,011)	(14,809,796)
Premiums/discounts	19,384,469	11,408,668	5,089,163	25,703,974
Totals	<u>\$ 692,204,215</u>	<u>\$ 111,158,115</u>	<u>\$ 151,033,152</u>	<u>\$ 652,329,178</u>

* - Includes \$109,185,000 of refunded bonds.

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS (cont.)

Revenue obligation serial and term bonds as of June 1, 2005 consisted of the following:

	<u>2005</u>
1991 Series 1:	
Term Bonds, mandatory redemption of bonds at 100% of par, June 1, 2009 through June 1, 2011	\$ 57,445,000
Unamortized discount on bonds	<u>(136,294)</u>
	<u>57,308,706</u>
1993 Series 2:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2004	30,780,000
Unamortized premium on bonds	<u>427,578</u>
	<u>31,207,578</u>
1997 Series 1:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2008	7,470,000
Unamortized premium on bonds	<u>104,466</u>
	<u>7,574,466</u>
1998 Series 1:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2008	31,385,000
Unamortized discount on bonds	<u>(90,531)</u>
	<u>31,294,469</u>
1998 Series 2:	
Serial Bonds, no optional redemption	90,400,000
Unamortized premium on bonds	<u>4,210,573</u>
	<u>94,610,573</u>
1999 Series 1:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2009	13,220,000
Unamortized (discount) premium on bonds	<u>31,126</u>
	<u>13,251,126</u>
2001 Series 1:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2011	41,535,000
Unamortized (discount) premium on bonds	<u>(82,101)</u>
	<u>41,452,899</u>
2002 Series 1:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2012	65,980,000
Unamortized premium on bonds	<u>376,465</u>
	<u>66,356,465</u>
2002 Series 2:	
Serial Bonds, no optional redemption	79,400,000
Unamortized premium on bonds	<u>4,276,733</u>
	<u>83,676,733</u>

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS (cont.)

	2005
2004 Series 1:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2014	\$ 116,795,000
Unamortized premium on bonds	5,552,364
	122,347,364
2004 Series 2:	
Serial Bonds, optional redemption for bonds at 100% of par, June 1, 2015	107,025,000
Unamortized premium on bonds	11,033,595
	118,058,595
Total of All Series	667,138,974
Unamortized deferred charge related to debt defeasance (Note 6)	(14,809,796)
Revenue Obligation Bonds, Net of Deferred Charge	\$ 652,329,178

The original issue discount or premium at issuance and the interest rates at June 1, 2005, on the following bond series were:

Series	Original Issue Discount/ (Premium)	Interest Rates
1991 Series 1	\$ 1,366,407	6.875%
1993 Series 2	(2,349,253)	4.75 – 6.125%
1995 Series 1	(1,253,936)	6.25%
1997 Series 1	(288,312)	5.25 – 6.00%
1998 Series 1	(811,362)	4.00 – 5.00%
1998 Series 2	(7,739,808)	4.00 – 5.50%
1999 Series 1	(58,061)	5.00 – 5.75%
2001 Series 1	(1,022,362)	4.50 – 5.25%
2002 Series 1	(2,426,001)	4.00 – 5.25%
2002 Series 2	(7,344,300)	3.00 – 5.50%
2004 Series 1	(6,632,300)	4.00 – 5.00%
2004 Series 2	(11,408,668)	3.25 – 5.25%

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 5 – REVENUE OBLIGATION BONDS AND RESTRICTED ASSETS (cont.)

Principal maturities of the bonds, net of advance refundings, as of June 1, 2005, are as follows:

Years Ending June 1,	Principal	Interest	Totals
2006	\$ 44,775,000	\$ 33,301,015	\$ 78,076,015
2007	47,085,000	30,906,521	77,991,521
2008	49,540,000	28,405,521	77,945,521
2009	52,020,000	26,111,359	78,131,359
2010	54,760,000	23,230,234	77,990,234
2011-2015	199,790,000	76,586,719	276,376,719
2016-2020	138,080,000	32,757,343	170,837,343
2021-2024	55,385,000	5,902,460	61,287,460
Totals	<u>\$ 641,435,000</u>	<u>\$ 257,201,172</u>	<u>\$ 898,636,172</u>

The revenue obligation bonds are collateralized by a security interest in all assets of the Leveraged Loan Portfolio. At June 1, 2005, the total assets of the Leveraged Loan Portfolio were \$825,243,101. Neither the full faith and credit nor the taxing power of the State is pledged for the payment of the revenue obligation bonds. However, as the loans granted to the municipalities are at an interest rate which is less than the Revenue Bond rate, the State is obligated by the Clean Water Fund General Resolution to fund, prior to each loan disbursement, a reserve, which subsidizes the Leveraged Loan Portfolio in an amount to offset this interest rate disparity.

Among other restrictions under the revenue obligation bond agreements are provisions that require that a specified amount of cash and investments be held by an independent trustee in a reserve account for the purpose of paying bond interest and principal when due. The restricted assets on the balance sheets consist of substantially all of the MBIA, AIG, Bayerische Landesbank investments (Note 3) and \$15 million of the LGIP balance held as a credit reserve. These amounts are required in order to satisfy the conditions of certain agreements related to maintaining the minimum credit ratings on the bonds.

NOTE 6 – ADVANCE REFUNDING

In 1993, the Fund defeased a portion of its 1991 Series 1 bonds through the issuance of 1993 Series 2 Refunding Bonds. The proceeds from the 1993 Series 2 Refunding Bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 1, 2005, there was \$47,110,000 of the defeased bonds outstanding that will be serviced by the irrevocable trust's remaining funds.

In 1998, the Fund defeased a portion of its 1991 Series 1, 1993 Series 1, 1995 Series 1 and 1997 Series 1 bonds through the issuance of \$104,360,000 of 1998 Series 2 Refunding Bonds. The proceeds from the 1998 Series 2 Refunding Bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 1, 2005, there was \$91,985,000 of the defeased bonds outstanding that will be serviced by the irrevocable trust's remaining funds.

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 6 – ADVANCE REFUNDING (cont.)

In 2002, the Fund defeased a portion of its 1993 Series 1, 1995 Series 1, 1997 Series 1, 1998 Series 1, and 1999 Series 1 bonds through the issuance of \$85,575,000 of 2002 Series 2 Refunding Bonds. The proceeds from the 2002 Series 2 Refunding Bonds were placed in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust assets and the liability for the defeased bonds are not included in the Fund's financial statements. At June 1, 2005, there was \$81,405,000 of the defeased bonds outstanding that will be serviced by the irrevocable trust's remaining funds.

On January 25, 2005, the Fund issued \$107,025,000 in revenue bonds with an average interest rate of 5.11 percent to advance refund \$109,185,000 of its 1998 Series 1, 1999 Series 1, 2001 Series 1, and 2002 Series 1 bonds with an average interest rate of 5.24 percent. The net proceeds of \$117,380,148 (after payment of \$1,048,855 in underwriting fees, insurance and other issuance costs) were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the refunded bonds. As a result, this portion of the bonds are considered to be defeased and the liability for those bonds has been removed from these financial statements.

The cash flow requirements on the refunded bonds and notes prior to the advance refunding was \$166,111,690 from 2005 through 2020. The cash flow requirements on the 2005 refunding bonds are \$160,718,638 from 2005 through 2020. The advance refunding resulted in an economic gain (difference between the present values of the debt service payments on the old and new debt) of \$4,251,744.

NOTE 7 – TRANSFERS IN

Transfers in consist of contributions from the State of Wisconsin. The full faith, credit and taxing power of the State are irrevocably pledged for payment of the principal of and interest on the Global Certificate.

In April 2004, all of the State of Wisconsin General Obligation Bonds previously owned by the Fund were exchanged for \$116,840,689 (par value) of State of Wisconsin General Obligation Bond, Clean Water Fund Program ("Global Certificate"). The estimated market value and weighted average coupon interest rate of the Global Certificate at June 1, 2005 is \$145,944,883 and 6.82%, respectively. The Bonds are registered in the name of the Fund and held by an independent trustee.

The Bond is registered in the name of the Portfolio and held by an independent trustee. By GASB Statement No. 3 definition, this security is classified as category one (insured or registered securities held by the Portfolio's agent in the Portfolio's name).

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 7 – TRANSFERS IN (cont.)

Principal maturities of the Global Certificate as of June 1 are as follows:

Years Ending June 1,	2005
2006	\$ -
2007	-
2008	-
2009	-
2010	14,518,075
2011-2015	45,467,534
2016-2020	36,726,010
2021-2024	20,129,070
Total	\$ 116,840,689

NOTE 8 – INVESTMENT INCOME

Investment income is recorded net of estimated required arbitrage relating to outstanding State of Wisconsin Clean Water Revenue Bonds and consisted of the following for the fiscal year ended June 1, 2005:

Interest:

State of Wisconsin Investment Board Local Government Investment Pool	\$ 1,471,581
MBIA Guaranteed Investment Agreement	387,518
Repurchase Agreement with Bayerische Landesbank	493,864
AIG Guaranteed Investment Agreement	1,769,209
United States Treasury Notes	1,307,178
Total Interest	5,429,350

Changes in Unrealized Gains (Losses);

State of Wisconsin Investment Board Local Government Investment Pool	
United States Treasury Notes	157,817
State of Wisconsin General Obligation Bonds	12,421,255
Total Changes in Unrealized Gains (Losses)	12,579,072

Total Interest and Changes in Unrealized Gains (Losses)	18,008,422
---	------------

Change in Estimated Rebtable Arbitrage Liability	(90,514)
--	----------

TOTAL INVESTMENT INCOME	\$ 17,917,908
-------------------------	---------------

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

NOTES TO FINANCIAL STATEMENTS For the Year Ended June 1, 2005

NOTE 9 – TRANSACTIONS WITH RELATED PARTIES

The DNR and DOA have statutory duties to manage the Portfolio. Expenses relating to the management of the Program are allocated to and paid by the Portfolio. Total allocated expenses from DNR and DOA, which are reflected in the statement of revenues, expenses and changes in net assets for the year ended June 1, 2005, were \$2,036,497.

The following details total salaries and benefits by agency for the fiscal year ended June 1, 2005:

DNR	\$ 1,240,369
DOA	<u>464,942</u>
Total	<u>\$ 1,705,311</u>

STATE OF WISCONSIN LEVERAGED LOAN PORTFOLIO

OTHER INFORMATION (UNAUDITED)
For the Year Ended June 1, 2005

In management's opinion, the Governmental Accounting Standards Board (GASB) does not require an MD&A for individual fund reports under GASB Statement No. 34, Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. Therefore, the State has not prepared an MD&A for the State of Wisconsin Leveraged Loan Portfolio. An MD&A is included in the Comprehensive Annual Financial Report for the State of Wisconsin, which includes all funds and component units.