



DEPARTMENT OF  
**ECOLOGY**  
State of Washington

# **Implementing the Water Pollution Control Revolving Administration Account**

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# REPORT TO THE LEGISLATURE



## Implementing the Water Pollution Control Revolving Administration Account

### Executive Summary

In response to impending federal cuts, Washington’s Legislature passed House Bill 1141 during the 2013 legislative session (codified as RCW 90.50A.090) that authorized a new Water Pollution Control Revolving Administration Account (564), (referred to as the administration fund), and established an administration charge to ensure ongoing funding to manage the Water Pollution Control Revolving Fund, also known as the Clean Water State Revolving Fund (CWSRF).

RCW 90.50A.090 (9) RCW includes the following text requiring this legislative report:

“By December 1, 2018, the Department (Ecology) must submit to the appropriate legislative fiscal committees a report on implementation of the administration charge, including information on: the amount of income the administration charge has produced since its inception; the uses and adequacy of the income for administrative costs; any excess balances that have been transferred to the Water Pollution Control Revolving Fund; and any additional sources that the department is using for program administration.”

Ecology is authorized to use the administration account for financial and engineering expertise as well as performance of day-to-day work associated with managing CWSRF loans for high-priority water quality projects. Additional authorized costs include the cost of financial information systems that support the management of the loan portfolio.

Ecology is currently charging a one percent administration charge on the declining balance of loans to fund the cost of administering the loan program, at no additional cost to the borrowers, on loans entering repayment starting in 2014. As more loans enter repayment, the income collected has grown to over \$2.2 million in 2018.

Ecology finds that the income it is collecting is now adequate to fund the administration of the loan program, following a period of transition from the Environmental Protection Agency (EPA) capitalization grant that allowed Ecology to use four percent of its grant award for administration. The four percent from the capitalization grant previously used for program administration will now be used for making loans to high priority projects moving forward.

Ecology estimates there will be a \$4.7 million balance in the administration fund at the end of the 2017-19 biennium. This figure assumes that, once the numbers for the biennium are finalized in September of 2019, any excess revenue beyond what is needed for working capital reserve will be transferred to the Water Pollution Control Revolving Fund to be used to award loans for high priority water quality projects.

Currently, the one percent administration charge to loan borrowers is more than adequate to cover the cost to administer the program going forward. Ecology will re-evaluate the loan charge percentage at the end of the 2017-19 biennium and make any necessary adjustments.

## **Background**

The Water Pollution Control Revolving Fund, also known as the Clean Water State Revolving Fund (CWSRF) loan program was established by the Clean Water Act and is funded by an annual Environmental Protection Agency (EPA) capitalization grant based on congressional appropriation, state matching funds, and principal and interest repayments on past CWSRF loans.

Ecology faced a deficit in the 2013-15 biennium in the EPA capitalization grant administration funds it used to manage the CWSRF loan program. This deficit posed a risk to Ecology's ability to effectively manage its loan program, which passes along essential financing to local governments for infrastructure projects that protect water quality in the state.

The CWSRF is a long-standing successful program that provides low-interest loans and forgivable principal loans (money that does not have to be paid back) to local governments, tribes and special purpose districts. The funding pays for wastewater and stormwater facility construction projects, nonpoint source pollution control projects, and environmentally sustainable (green) projects. Ecology manages this program in accordance with federal regulation CFR 40.35.3100 and state regulation RCW 90.50A.090. The governing statute links are included in the reference section of this report.

Ecology is allowed to use up to four percent of the federal capitalization grant to cover its costs to administer the program. The Clean Water Act does not allow Ecology to use any repayments of principal and interest to administer the CWSRF loan program.

If the trends had remained unchanged, Ecology faced a deficit in its CWSRF administration funds in state fiscal year 2014 and beyond, due to reductions of the federal capitalization grant.

In March of 2013, the Legislature passed Substitute House Bill 1141, establishing a Water Pollution Control Revolving Loan Administration Charge, which gave Ecology statutory authority to assess a loan administration charge to pay for the costs to administer the CWSRF loan program. This bill protects Washington against the fluctuation of federal funding, sets the CWSRF fund as self-sustaining in perpetuity, and maintains a critical loan program that protects water quality in Washington.

The administration charge does not increase the debt service (cost to borrowers) beyond what the borrower would otherwise already pay under current rule and process.

The CWSRF loan debt service interest rate for standard 20-year term loans is 60 percent of the market rate for tax-exempt municipal bonds. To prevent additional costs to borrowers, Ecology lowered the interest rate on loans and added a loan administration charge. The interest charged and the administration charge together comprise the debt service of the loan, and it does not exceed 60 percent of the average rate for tax exempt municipal bonds. Loan rates are established annually at the beginning of each funding cycle set annually per rule WAC 173-98.

## Authorized Uses of the Administration Fund

Ecology uses the administration fund to provide technical and financial assistance to local governments who are awarded funding for wastewater and stormwater facilities and nonpoint source activities projects with CWSRF loan funds. The authorized uses are set forth in RCW 90.50A.090 and Ecology adheres to the authorized uses which include engineers that provide technical assistance and oversight, review, and approval of engineering documents for wastewater and stormwater facilities; staff who provide wastewater and stormwater facility site inspections; the management of complicated wastewater and stormwater facility projects; as well as nonpoint source activities projects. Ecology also uses the administration fund to provide strategic financial planning and performance analysis of the CWSRF loan portfolio. Additional authorized uses include the costs of financial systems that help CWSRF staff manage the loan portfolio, including a loan tracking and payables system.

Ecology plans to replace its existing outdated loan tracking and receivables system with a new system that will provide modern industry standard technology, for the management of the CWSRF loan portfolio. The project funding includes approximately \$425,000 from the administration fund and the remaining \$1.8 million in funding will come from other Ecology program contributions. The new system is expected to be in place by July of 2019.

## Summary of Income

Ecology is currently charging one percent on the declining principal loan balance to fund the cost of administering the CWSRF loan program. The administration charge does not increase the debt service (cost to borrowers) beyond what the borrower would otherwise already pay. Loans subject to the administration charge began to enter repayment in 2014. As more loans continue to enter repayment each year, the revenue collected continues to increase. Since inception, Ecology has collected a total of \$6.6 million in administration charges, as of June 30, 2018.

The fees collected for the administration fund since its inception are as follows:

	<b>Fiscal Year</b>				
	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
Administration Fee Collected	15,278	1,189,363	1,217,791	1,848,760	2,250,957
Interest on admin fee collected	5	1,129	10,826	21,476	46,845
<b>Total Revenue</b>	<b>15,283</b>	<b>1,190,492</b>	<b>1,228,617</b>	<b>1,870,236</b>	<b>2,297,802</b>
 <i>Cumulative Revenue Total</i>		<i>1,205,775</i>	<i>2,434,393</i>	<i>4,304,628</i>	<i>6,602,430</i>

## Adequacy of Income and Other Fund Sources

Ecology began collecting the administration charge on loans entering repayment in January of 2014 and realized that due to the timing of loan repayments in Fiscal Year (FY) 2014 and 2015, there would be a slower transition to the administration fund than originally anticipated.

Based on existing balances from the EPA capitalization grant 4 percent administration set aside, Ecology was able to fully fund the administration costs of the CWSRF loan program in the first two years of revenue collections.

Beginning in FY 2016 and 2017, the administration fund began to support a portion of the administration costs for the loan program, and in FY 2018 the administration costs were fully supported by the administration fund.

The following table shows the history of both the Water Pollution Control Revolving Administration Account (564) and the EPA capitalization grant administration portion of the Water Pollution Control Revolving Account (727) along with incurred operating expenses, since the inception of the administration fund in FY 2014:

### Water Pollution Control Revolving Administration Account (564)

	Fiscal Year				
	2014	2015	2016	2017	2018
Administration Fee Collected	15,278	1,189,363	1,217,791	1,848,760	2,250,957
Interest on admin fee collected	5	1,129	10,826	21,476	46,845
<b>Total Revenue</b>	<b>15,283</b>	<b>1,190,492</b>	<b>1,228,617</b>	<b>1,870,236</b>	<b>2,297,802</b>
Total Operating expenses incurred (564)	0	0	26,311	256,344	1,749,702

### EPA Capitalization Grant Administration Portion of the Water Pollution Control Revolving Account (727)

	Fiscal Year				
	2014	2015	2016	2017	2018
Admin - Fed Awarded	774,861	812,734	808,568	774,469	124,578
Admin - State Match	156,125	162,586	161,752	154,931	24,922
Total Admin Available	930,986	975,320	970,320	929,400	149,500
Admin Drawn	930,986	975,320	970,320	654,025	0
Unspent Cap Grant Admin	0	0	0	275,375	149,500
Total Operating expenses incurred (727)	1,308,811	1,260,708	1,467,697	1,196,876	0

## Administration Fund Balance

Ecology estimates the ending balance of the administration fund will be \$191,000 at the end of the 2017-19 biennium after transferring an estimated \$4.5 million to the CWSRF Fund. The following shows the breakdown of the balance:

### Estimated Fund Balance Administration Account (564)

Dollars in thousands	2017-19	2019-21
<b>BEGINNING FUND BALANCE (July 1, 2017)</b>	<b>\$4,022</b>	<b>\$4,691</b>
<b>REVENUE</b>		
<b>Ecology Revenue</b>		
Loan Admin Charge	<b>\$4,500</b>	<b>\$4,770</b>
<b>Other Revenue</b>		
Interest Income	\$68	\$68
<b>Total Revenue</b>	<b>\$4,568</b>	<b>\$4,838</b>
<b>PROPOSED TRANSFERS</b>		
Water Pollution Control Account (Fund 727)		(\$4,500)
<b>Total Transfers</b>	<b>\$</b>	<b>(\$4,500)</b>
<b>OPERATING</b>		
<b>Ecology</b>		
Carryforward	\$1,652	\$3,651
Maintenance Level	\$31	
Performance Level	\$1,918	
2018 Supplemental	(\$6)	
Agency Request 2019 Supplemental	<b>\$4</b>	
Agency Request 2019-21		<b>\$210</b>
<b>Enacted 2017-19 Budget</b>		
<b>Total Operating</b>	<b>\$3,599</b>	<b>\$3,861</b>
<b>ENDING FUND BALANCE</b>		
Working Capital Reserve	(\$300)	(\$300)
<b>ENDING FUND BALANCE</b>	<b>\$4,691</b>	<b>\$868</b>

## Next Steps

Ecology will confirm the administration fund final balance at the end of the 2017-19 biennium and take the following actions:

- Ecology may find that there is an excess balance on June 30, 2019, in the administration account, and after deducting an adequate working capital reserve of \$300,000, the remaining balance would be transferred to the CWSRF loan fund and used for loans. The proposed transfer from the administration fund to the CWSRF loan fund, based on the projected fund balance, is \$4.5 million. This would be the first time such a transfer would take place between the two accounts.
- Ecology, through evaluation and analysis of the administration charge rate, may find that the one percent administration charge to CWSRF loan borrowers is more than needed to adequately cover the cost of administering the program going forward. Ecology would then reduce the administration charge to a new rate informed by analysis and fund projections, and at the same time increase the interest rate so that together the borrower would be paying 60 percent of the market rate for tax-exempt municipal bonds on loans entering repayment. This would maintain the same effective interest rate at no additional costs to borrowers. Reducing the administration charge would shift more funds through interest income back into the CWSRF loan account to be used for priority project loans. This change would take place when the new loan tracking system is implemented to ensure a simple and effective change and integration with the new information system.

## Conclusion

Ecology finds that the income it is collecting is now adequate to fund the administration of the loan program, following a period of transition from the Environmental Protection Agency (EPA) capitalization grant that allowed Ecology to use four percent of its grant award for administration. The four percent from the capitalization grant previously used for program administration will be used for making loans to high priority projects moving forward. Ecology did not use any other fund sources for administration of CWSRF loan program.

Ecology estimates there will be a \$191,000 balance in the administration fund at the end of the 2017-19 biennium after setting aside the \$300,000 working capital reserve and the projected \$4.5 million transfer to the CWSRF fund, the transferred funds will be used to award loans for high priority water quality projects. Currently the one percent administration charge to loan borrowers is more than adequate to cover the cost to administer the program going forward. Ecology will re-evaluate the loan charge percentage at the end of the 2017-19 biennium and make any necessary adjustments.

## References

SRF 2018 Report

CFR 40.35

RCW 90.50A.090.

WAC 173-98-400(7).

## Publication information

This report is available on the Department of Ecology's website at <https://fortress.wa.gov/ecy/publications/SummaryPages/xxxxxxx.html>

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