

AGENDA (ANNOTATED)

**TENNESSEE LOCAL DEVELOPMENT AUTHORITY
AUDIT COMMITTEE
JUNE 25, 2020, 3PM
VIA ON-LINE MEETING (WEBEX)**

1. **(Treasurer)** Call Meeting to Order
2. **(Treasurer)** Statement of Necessity for Telephonic Participation *
3. **(Treasurer)** Approval of the AC Meeting Minutes June 27, 2019 **(Tab 1) ***
4. **(Derek Martin)** Review Audit Reports Issued by Comptroller's Office
 - a. Discuss TLDA Audit Report **(Tab 2, pages 5-33 meeting packet)**
 - b. Discuss Clean Water State Revolving Fund Audit Report **(Tab 2, pages 33-46 meeting packet)**
5. **(Alicia West)** Review Financial Statements including Significant Accounting & Reporting Standards **(Tab 3)**
6. **(Felicia Freeman)** Discuss Program Evaluation Reports (PERS) from EPA **(Tab 4)**
 - a. 2019 TN_SRF Drinking Water PERS Report **(Tab 4a)**
 - b. 2019 TN_SRF Clean Water PERS Report **(Tab 4b)**
7. **(Sandi Thompson)** Risk Assessments Memo **(Tab 5)**
 - a. 2019 SLF Risk Assessment **(Tab 5a)**
 - b. 2019 TDEC Water Resource Risk Assessment **(Tab 5b)**
8. **(Sandi Thompson)** Discuss Management's Responsibility to Prevent, Detect & Report Fraud, Waste & Abuse
9. **(Sandi Thompson)** Discuss Comptroller Hotline
10. **(Earle Pierce)** Current Internal Auditing Article **(Tab 6)**
11. **(Treasurer)** Opportunity for Public Comment
12. **(Treasurer)** Other Business
13. **(Treasurer)** Adjournment

* Items with an asterisk denote action required by the Audit Committee

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
AUDIT COMMITTEE MEETING MINUTES
June 27, 2019

The Tennessee Local Development Authority (TLDA) Audit Committee met on Thursday, June 27, 2019. The meeting began at 10:30 a.m. in the Cordell Hull Building, House Hearing Room III.

The following members were present:

- David H. Lillard, Jr., State Treasurer
- Dr. Kenneth Moore, House Appointee
- Angela Scott, Delegate for Stuart McWhorter, Commissioner of Finance and Administration
- Tre Hargett, Tennessee Secretary of State
- Pat Wolfe, Senate Appointee

Others present were:

- Sandi Thompson, Director, Office of State and Local Finance
- Leslie Gillespie-Marthaler, Director of State Revolving Fund Program, TN Department of Environment and Conservation (TDEC)
- Derek Martin, State Auditor, Office of the Comptroller of the Treasury
- Earle Pierce, Director of Internal Audit, TN Department of Treasury
- Paula Mitchell, TN Department of Environment and Conservation (TDEC)

Call Meeting to Order

Treasurer Lillard called the meeting to order noting a quorum and presented the minutes from the May 16, 2018 TLDA Audit Committee meeting for approval. There were no other recommended changes. Dr. Kenneth Moore motioned to accept the minutes as presented and Secretary Hargett seconded the motion. Mr. Pierce performed a roll-call vote:

Treasurer Lillard, Aye; Secretary Hargett, Aye; Dr. Kenneth Moore, Aye; Angela Scott, Aye; Mr. Wolfe, Aye.

Revised TLDA Audit Committee Charter

Mr. Pierce presented a revised Audit Committee charter for the Committee to consider and adopt. Mr. Pierce noted the last revision of the charter took place in 2009. The charter revisions were based upon the Tennessee Comptroller guidelines for audit committee charters as well as best practices of the Institute of Internal Auditors. Mr. Pierce noted the revised charter had already been approved by the TN Comptroller. Secretary Hargett made a motion to approve the

revised Audit Committee charter and Dr. Kenneth Moore seconded the motion. Mr. Pierce performed a roll-call vote:

Treasurer Lillard, Aye; Secretary Hargett, Aye; Dr. Kenneth Moore, Aye; Angela Scott, Aye; Mr. Wolfe, Aye.

Review Audit Reports Issued by Comptroller's Office

Treasurer Lillard recognized Derek Martin from State Audit to review the audit reports for the Tennessee Local Development Authority (TLDA) and the Clean Water State Revolving Fund (CWSRF). Both the TLDA and CWSRF received unmodified opinions on their June 30, 2018 financial statements. No material errors were found in the financial statements. There were no findings and no exceptions noted with internal controls or compliance.

Review Financial Statements Including Significant Accounting and Reporting Standards

Treasurer Lillard recognized Sandi Thompson to review the financial statements for the TLDA and the SRF programs. Ms. Thompson presented an overview of the financial statements.

Review of Program Evaluation Reports from the EPA

Treasurer Lillard recognized Leslie Gillespie-Marthaler, Director of the State Revolving Fund Program (SRF) from TDEC to discuss reports from the EPA. Ms. Gillespie-Marthaler reviewed Program Evaluation Reports (PERs) from the Environmental Protection Agency for studies conducted in fiscal year 2018 with reports dated as of December 2018. The reports covered the Clean Water State Revolving Fund and the Drinking Water State Revolving Fund. The 2018 PERs reports contained no findings or deficiencies. The reports included four recommendations for each program. Ms. Gillespie-Marthaler reviewed each of the recommendations with the Committee and the status of SRF's efforts to address them. Treasurer Lillard asked about the program's challenge in meeting the Disadvantaged Business Enterprises (DBE) goal. Ms. Gillespie-Marthaler outlined their attempts to encourage DBE participation noting smaller communities have less options for utilizing DBEs, but they will continue to work with smaller communities to increase DBE participation.

State and Local Finance 2018 Risk Assessments

Treasurer Lillard recognized Sandi Thompson to discuss the Office of State and Local Finance (SLF) and Division of Water Resources 2018 Risk Assessments. Ms. Thompson stated the risk assessments cover risks and controls as required by the Financial Integrity Act. A memo regarding the act was included in the materials. Ms. Thompson discussed some of the testing performed to ensure controls documented in the risk assessments worked as intended.

Discuss Management's Responsibility to Prevent, Detect and Report Fraud, Waste and Abuse

Treasurer Lillard recognized Sandi Thompson to speak about management's responsibility to prevent, detect, and report fraud, waste, and abuse. Ms. Thompson stated the tone at the top is the first line of defense for preventing fraud, waste, and abuse. Ms. Thompson noted she was not aware of any instances of reported fraud, waste, or abuse within the Office of State and Local Finance. Department personnel are aware risk exists with performing their duties. Those risks are monitored and mitigated daily. The annual risk assessment and system of controls is updated when necessary to alleviate risks.

Discuss Comptroller Hotline

Treasurer Lillard recognized Sandi Thompson to discuss the Comptroller's Fraud, Waste, and Abuse (FWA) Hotline. Ms. Thompson noted they do receive calls on their hotline and forward them to their investigations division when appropriate.

Discuss Current Internal Audit Article

Treasurer Lillard recognized Earle Pierce to present a Tone at the Top article from the Institute of Internal Auditors entitled, "Generating and Bringing Accurate Information to the Board". Mr. Pierce summarized the article with a brief discussion on Board challenges in monitoring risk, the challenge of management to employ systems and channels providing Boards with accurate information. Mr. Pierce's summary included a review of action items organization need to take in order to present accurate information to the board.

Other Business

Treasurer Lillard opened the floor for any other business to be brought before the Committee. No new business was presented.

Adjournment

Treasurer Lillard asked for a motion to adjourn. Dr. Kenneth Moore made a motion to adjourn. Angela Scott seconded the motion. Treasurer Lillard adjourned the meeting.

Approved:

David H. Lillard, Jr.
TLDA Audit Committee Chairman



FINANCIAL AND COMPLIANCE AUDIT REPORT

Tennessee Local Development Authority

For the Year Ended June 30, 2019

Justin P. Wilson
Comptroller of the Treasury



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Mission Statement
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make government work better.

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JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

February 13, 2020

The Honorable Bill Lee, Governor
Members of the General Assembly
Members of the Tennessee Local Development Authority

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Tennessee Local Development Authority for the year ended June 30, 2019. You will note from the independent auditor's report that an unmodified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

A handwritten signature in black ink that reads "Deborah V. Loveless".

Deborah V. Loveless, CPA, Director
Division of State Audit

20/013

Audit Report
Tennessee Local Development Authority
For the Year Ended June 30, 2019

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State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit

Tennessee Local Development Authority

For the Year Ended June 30, 2019

Opinion on the Financial Statements

The opinion on the financial statements is unmodified.

Audit Findings

The audit report contains no findings.



JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

Independent Auditor's Report

The Honorable Bill Lee, Governor
Members of the General Assembly
Members of the Tennessee Local Development Authority

Report on the Financial Statements

We have audited the accompanying financial statements of the Tennessee Local Development Authority, a component unit of the State of Tennessee, as of and for the years ended June 30, 2019, and June 30, 2018, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used

and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of the Tennessee Local Development Authority. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Authority.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Tennessee Local Development Authority as of June 30, 2019, and June 30, 2018, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information


Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, on pages 5 through 10, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Authority's basic financial statements. The accompanying financial information on pages 20 through 22 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the basic financial statements. The information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 17, 2020, on our consideration of the Tennessee Local Development Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts (including the bond resolutions) and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance.



Deborah V. Loveless, CPA, Director
Division of State Audit
January 17, 2020

TENNESSEE LOCAL DEVELOPMENT AUTHORITY

Management's Discussion and Analysis

As management of the Tennessee Local Development Authority, we offer readers of the Authority's basic financial statements this narrative overview and analysis of the financial activities of the Authority for the fiscal years ended June 30, 2019, and June 30, 2018, with comparative data for the year ended June 30, 2017. This discussion has been prepared by management along with the financial statements and related note disclosures and should be read in conjunction with the Independent Auditor's Report, the audited financial statements, and the accompanying notes. The financial statements, notes, and this discussion are the responsibility of management.

Program Activity Highlights

The Authority's purpose is to provide loans to local government units under the State Loan Program and the State Infrastructure Program. The table below summarizes this business activity.

Pursuant to Title 4, Chapter 31, *Tennessee Code Annotated*, the General Assembly of the state created the Tennessee Local Development Authority to issue bonds and notes to fund capital projects for a variety of purposes. Currently, the programs of the Authority which have made loans to borrowers include

- 1) the State Loan Program, which provides assistance to local government units in the construction of waterworks, sewage treatment, and energy and/or solid waste recovery facilities, and
- 2) the State Infrastructure Program, which provides assistance to local government units in the construction of transportation infrastructure projects that provide public benefits by enhancing mobility or safety, promoting economic development, or increasing the quality of life and general welfare of the public.

	Local			State		
	Government Units			Infrastructure Program		
	2019	2018	2017	2019	2018	2017
Number of borrowers with outstanding loans	5	8	10	1	1	1
Total number of outstanding loans	7	10	12	1	1	1
Total amount of outstanding loans (in thousands)	\$1,494	\$1,891	\$2,311	\$1,490	\$1,126	\$211
Number of outstanding loans approved in fiscal year	0	0	0	0	0	0
Amount of loans approved in fiscal year (in thousands)	\$0	\$0	\$0	\$0	\$0	\$0

The state is not liable on any debt of the Authority, and the bonds are not a debt of the State of Tennessee. For more specific financial information on long-term debt activity, see Note 5, Debt Payable, in the notes to the financial statements.

The financial statements and the analysis provided in the remainder of this report reflect the financial results of this activity.

Debt Administration

The Authority's most long-standing program is its State Loan Program. To date, the State Loan Program has only been utilized to make loans for the construction of water and sewer projects. A financial analysis is conducted for each loan applicant to be funded through the State Loan Program before the application is approved by the Authority. Each local government unit must demonstrate that it has enacted rates and charges sufficient to repay the debt, as well as to fund operations, maintenance, and depreciation. The Authority also compares state-shared taxes, which are pledged by the local government unit, in relation to projected debt service. The Authority is authorized to intercept these state-shared taxes, should the government unit fail to timely repay its loan. The balance of any deficit would be secured by the debt service reserve fund and the statutory reserve fund. The statutory reserve fund is an amount set aside in the fund from appropriations of the state's General Assembly from 1985 to 1987, intended to ensure payment of debt service on debt issued for any purpose under the State Loan Program.

During its construction phase, a project in the State Loan Program is typically funded through the issuance of Bond Anticipation Notes. When a sufficient dollar amount of projects are completed to assure an appropriate economy of scale to sell bonds, the Authority may fix the interest rate for the term of the projects by issuing long-term debt. Interest rates on the State Loan Program facilities long-term fixed-rate debt range from a low of 4.00% to a high of 4.375%. By pooling the financing of their capital needs, management believes that economic efficiencies of a single large borrowing administered by one agency are achieved. The creditworthiness of both large and small local government units is blended into one credit resulting in a lower cost of borrowing to most participants.

At June 30, 2019, the Authority's State Loan Program is rated AA+/Negative by Standard & Poor's Rating Group (S&P) and AA by Fitch Ratings. On May 28, 2019, S&P placed the AA+ rating on credit watch with negative implications. The credit watch reflects the decline in the number of participants in the pool as the program has wound down. On October 1, 2019, S&P subsequently downgraded the rating to AA and removed the credit watch. The downgrade reflects S&P's assessment of the bonds based on the application of its "Issue Credit Ratings Linked to U.S. Public Finance Obligors' Creditworthiness" criteria. In general, rating reports include comments about the Authority's ongoing commitment to conservative practices, as well as sound legal provisions, strong state oversight, and an ample debt service reserve as strengths of the credit. Rating agencies also note that added strengths of the credit of the program are the underlying credit quality of the local governments receiving loans, the responsibility of the localities to repay loans, and the Authority's history of never needing to intercept state-shared taxes or tap the statutory reserve fund.

The State Infrastructure Fund was created in 2009 with the transfer of the existing state infrastructure bank, which had been under the administration of the Tennessee Department of Transportation (TDOT). The following sources can be used to provide additional capitalization to the fund: appropriations from the state's General Assembly; federal funds apportioned and available to the state and approved by TDOT; contributions, donations, and grants from the federal government or other governmental units or private entities; and principal and interest repayments from the borrowers. The Authority reviews each loan application to determine the borrower's

capability to assure sufficient revenues to operate and maintain the project for its useful life and to repay the loan. The borrower may pledge its state-shared taxes, its full faith and credit and unlimited taxing power, or other security as the Authority deems appropriate. No debt may be issued in order to provide loans to borrowers from the State Infrastructure Fund. The Authority is charged with the responsibilities of approving loan applications and administering the loans. The Authority has received and approved one loan application from the fund.

Overview of the Financial Statements

The Authority is a discretely presented component unit of the State of Tennessee and uses proprietary fund accounting. The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America using the accrual basis of accounting and the flow of economic resources measurement focus. This basis recognizes revenues when earned and expenses at the time liabilities are incurred, regardless of the timing of related cash flows. Using the economic resources measurement focus, readers are presented information that allows them to determine the transactions and events that have increased or decreased the total economic resources for the period.

This discussion and analysis is intended to serve as an introduction to the Authority's basic financial statements. The Authority's basic financial statements consist of two components: 1) the financial statements and 2) the notes to the financial statements. The financial statements consist of the statement of net position; the statement of revenues, expenses, and changes in net position; and the statement of cash flows. The statement of net position reports the Authority's overall financial position at June 30, the end of each fiscal year presented. The statement of revenues, expenses, and changes in net position reports the results of operations for the year. The statement of cash flows summarizes the inflows and outflows of cash throughout the fiscal year. These statements are supplemented by notes to the financial statements, which provide information essential to the reader's understanding of the financial statements. In addition to the financial statements and notes, this report also contains supplementary information containing financial statement information at the program level.

Financial Analysis of the Authority

Standard indicators of financial success are not applicable to the Authority. The financial goal of the Authority is to provide timely access to the capital markets at the lowest possible cost and to make creditworthy loans. There have been no incidents which required the Authority to refuse a loan application due to the inability to obtain capital funding. Also, the Authority has never had to use the intercept of state-shared taxes, nor has it had to draw from the debt service reserve fund or the statutory reserve fund in order to pay debt service.

The following is a discussion highlighting certain elements of the Authority's financial statements.

Statements of Net Position Summary
(in thousands of dollars)

	<u>2019</u>	<u>2018</u>	<u>2017</u>
Current assets	\$15,363	\$15,115	\$15,655
Restricted assets	515	595	709
Other assets	2,663	2,628	2,058
Total assets	18,541	18,338	18,422
Deferred outflows of resources	64	102	141
Current liabilities	605	656	697
Noncurrent liabilities	1,567	2,026	2,545
Total liabilities	2,172	2,682	3,242
Net position (unrestricted)	\$16,433	\$15,758	\$15,321

Note: The Authority owns no capital assets.

For the years ended June 30, 2019; June 30, 2018; and June 30, 2017, the largest component of the total asset balance is the cash balance. Loans receivable (both current and noncurrent) totaled \$2,983,522 at June 30, 2019; \$3,017,833 at June 30, 2018; and \$2,522,871 at June 30, 2017. Restricted assets represent the debt service reserve fund. Other assets slightly increased each year due to disbursements made to the one borrower in the State Infrastructure Fund; however, over time it is expected to trend downward unless new loans are made. The Authority's liabilities consist mostly of the outstanding portion of its bonds payable. No bonds have been issued since 2006. No Revenue Bond Anticipation Notes were issued during any of the three years presented. The Authority has not received any loan applications in the current fiscal year and, therefore, has no plans to issue debt in the immediate future. In the current market, communities who have previously utilized the program have identified other funding opportunities that better suit their needs at this time.

Statements of Revenues, Expenses, and Changes in Net Position Summary
(in thousands of dollars)

	<u>2019</u>	<u>2018</u>	<u>2017</u>
Operating Revenues			
Revenue from loans	\$121	\$111	\$130
Administrative fees collected	443	378	264
Interest income	343	203	83
Total operating revenues	907	692	477
Operating Expenses			
Interest expense	108	131	163
Subsidy to borrowers	13	13	-
Administrative expenses	111	111	110
Total operating expenses	232	255	273
Operating income	675	437	204
Increase in Net Position	\$675	\$437	\$204

The Authority's operating expenses are supported by revenue received from the borrowers as a one-time cost of issuance expense not to exceed 2% at the time of permanent financing, interest on loans, and income on investments. In addition, the Authority has oversight and approval duties related to loans made from the Clean Water and Drinking Water State Revolving Fund (SRF) programs. In 2010, the Authority was given statutory authority to charge the SRF borrowers a fee for the administration of the loans. Therefore, subsequent loans approved are charged an eight-basis point (0.08%) fee on the outstanding balance of the loan over its life. These administrative fees are recognized by the Authority as operating revenue. Operating expenses include interest expense on outstanding debt and administrative expenses of the program. A portion of investment earnings will be returned to borrowers as a subsidy to borrowers upon bond maturity.

Revenue to the Authority increased from 2018 to 2019 and also from 2017 to 2018. The increase in total operating revenues is mainly attributed to administrative fees collected on SRF program loans. Improved market interest rates were responsible for an increase in interest earned on the Authority's investments. Meanwhile, revenue from loans of the Authority is declining. All of the Authority's loans are structured such that the borrowers pay level debt service payments for the life of the loan, meaning that over time the borrowers' principal payment will increase, and the interest payment will decrease. Since no new loans have been made, as the existing loans approach maturity, the interest revenue will trend downward. The Authority's total operating expenses decreased from 2018 to 2019 and from 2017 to 2018. Unless new loans are made, operating expenses will continue to trend downward.

Contacting the Authority's Management Team

This discussion and analysis is designed to provide our citizens, local government units, community providers, investors, and creditors with a general overview of the Authority's finances and to demonstrate its accountability for the monies it receives. If you have questions about this report or need additional financial information, contact the Office of State and Local Finance, State of Tennessee, Cordell Hull Building, 425 Fifth Avenue North, Tennessee 37243-3400 or visit our website at www.comptroller.tn.gov/sl/.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Statements of Net Position
June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	June 30, 2019	June 30, 2018
Assets		
Current assets:		
Cash (Note 2)	\$15,042	\$14,726
Receivables:		
Loans receivable	321	389
Total current assets	15,363	15,115
Noncurrent assets:		
Restricted cash (Notes 2 and 3)	515	595
Loans receivable	2,663	2,628
Total noncurrent assets	3,178	3,223
Total assets	18,541	18,338
Deferred outflows of resources		
Deferred amount on bond refunding	64	102
Liabilities		
Current liabilities:		
Accrued interest payable	27	33
Payable to borrowers (Note 4)	143	128
Revenue bonds payable (Note 5)	435	495
Total current liabilities	605	656
Noncurrent liabilities:		
Revenue bonds payable, net (Note 5)	1,567	2,026
Total noncurrent liabilities	1,567	2,026
Total liabilities	2,172	2,682
Net position		
Unrestricted (Note 6)	16,433	15,758
Total net position	\$16,433	\$15,758

The notes to the financial statements are an integral part of this statement.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Statements of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	<u>Year Ended June 30, 2019</u>	<u>Year Ended June 30, 2018</u>
Operating revenues		
Revenue from loans	\$ 121	\$ 111
Administrative fees collected	443	378
Interest income	343	203
Total operating revenues	907	692
Operating expenses		
Interest expense	108	131
Subsidy to borrowers	13	13
Administrative expenses	111	111
Total operating expenses	232	255
Operating income	675	437
Net position		
Net position, July 1	15,758	15,321
Net position, June 30	\$16,433	\$15,758

The notes to the financial statements are an integral part of this statement.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Statements of Cash Flows
For the Years Ended June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	Year Ended June 30, 2019	Year Ended June 30, 2018
Cash flows from operating activities		
Payments to service providers	\$ (111)	\$ (111)
Net cash used by operating activities	(111)	(111)
Cash flows from noncapital financing activities		
Principal payments	(495)	(585)
Interest paid	(101)	(124)
Net cash used by noncapital financing activities	(596)	(709)
Cash flows from investing activities		
Loans issued	(364)	(915)
Collections of loan principal	400	464
Interest received on loans	121	111
Administrative revenue	443	378
Interest received on pooled investment fund	343	203
Net cash provided by investing activities	943	241
Net increase (decrease) in cash	236	(579)
Cash, July 1	15,321	15,900
Cash, June 30	\$15,557	\$15,321
Reconciliation of operating income to net cash used by operating activities:		
Operating income	\$ 675	\$ 437
Adjustments to reconcile operating income to net cash used by operating activities:		
Revenue from loans	(121)	(111)
Interest income	(343)	(203)
Interest expense	108	131
Subsidy to borrowers	13	13
Administrative revenue from borrowers	(443)	(378)
Total adjustments	(786)	(548)
Net cash used by operating activities	\$ (111)	\$ (111)

The notes to the financial statements are an integral part of this statement.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Notes to the Financial Statements
June 30, 2019, and June 30, 2018

Note 1. Summary of Significant Accounting Policies

Reporting Entity

The Tennessee Local Development Authority was created to provide financial assistance to local governments through the issuance of revenue bonds or notes. The Authority has also issued bonds to assist nonprofit corporations in the construction of mental health, mental retardation, or alcohol and drug facilities.

The Authority is a component unit of the State of Tennessee and is a separate legal entity. In accordance with the Governmental Accounting Standards Board's (GASB) Statement 14, *The Financial Reporting Entity*, as amended, the Authority is discretely presented in Tennessee's *Comprehensive Annual Financial Report* because the Authority's board consists of state officials which include the Governor, the Secretary of State, the Comptroller of the Treasury, the State Treasurer, the Commissioner of Finance and Administration, a State Senate appointee, and a State House appointee. The Governor serves as chairman, and the Secretary of State serves as vice chairman. The Comptroller of the Treasury serves as secretary. The Director of the Office of State and Local Finance serves as the assistant secretary; the Office of State and Local Finance provides administrative and financial services to the Authority. Therefore, the state has the ability to affect the day-to-day operations of the Authority.

The Authority does not have any employees. The members serve without salary but are entitled to reimbursement for their actual and necessary expenses incurred in the performance of their official duty.

Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Measurement Focus and Basis of Accounting

The accompanying financial statements have been prepared using the accrual basis of accounting and the flow of economic resources measurement focus. Under this basis, revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred, regardless of the timing of related cash flows.

The Tennessee Local Development Authority distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with principal ongoing operations. The Authority's principal operation is to provide loans to local governments through the issuance of revenue bonds or notes. Therefore, the principal operating revenues of the Authority are from

Notes to the Financial Statements (Continued)

interest on loans made to borrowers. The Authority also recognizes income on investments as operating revenue. The Authority's operating expenses include interest paid on borrowings, subsidies to borrowers, bond issuance costs, arbitrage, and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash

This classification includes cash on hand and deposits in the pooled investment fund administered by the State Treasurer.

Bond Discounts, Bond Premiums, and Issuance Costs

Bond discounts and premiums are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable unamortized bond discounts and premiums. Bond issuance costs are expensed when incurred.

Note 2. Deposits

Under the general bond resolution of the Tennessee Local Development Authority, the funds of the Authority are to be held and invested by the State Treasurer.

The Authority does not utilize its own bank accounts but has cash on deposit for its operating cash purposes in the State Pooled Investment Fund administered by the State Treasurer. The Authority had \$15,557,957 in the pooled investment fund at June 30, 2019, and \$15,321,385 at June 30, 2018. The pooled investment fund is authorized by statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The funds are very liquid; there are no minimum amounts or lengths of time for investment. The fund is not rated by a nationally recognized statistical rating organization. The fund's investments are measured at amortized cost. Its investment policy and required risk disclosures are presented in the *State of Tennessee's Treasurer's Report*. The report is posted on the state's website at <https://treasury.tn.gov/>.

Note 3. Restricted Assets

The general bond resolution of the Authority requires that the principal of each bond issue include an amount equal to one year's debt service requirement and that such amount be placed in special trust accounts with the trustee. The required debt service reserve was \$515,690 at June 30, 2019, and \$595,490 at June 30, 2018.

Note 4. Payable to Borrowers

This account represents interest earnings on restricted assets and loan principal that is being held until the bonds mature and then will be refunded to borrowers.

Notes to the Financial Statements (Continued)

Note 5. Debt Payable

Revenue Bonds

Bonds payable at June 30, 2019, and June 30, 2018, were as follows (expressed in thousands):

	<u>June 30, 2019</u>	<u>June 30, 2018</u>
2006 Refunding Series A at interest rates of 4% maturing to 2021 (original par-\$20,070)	\$ 310	\$ 610
2006 Series B at interest rates from 4% to 4.375% maturing to 2029 (original par-\$37,415)	<u>1,660</u>	<u>1,855</u>
Total par amount of bonds payable	1,970	2,465
Plus unamortized premium	40	65
Less unamortized discount	<u>(8)</u>	<u>(9)</u>
Net bonds payable	<u>\$2,002</u>	<u>\$2,521</u>

Debt service requirements to maturity of the revenue bonds payable at June 30, 2019, were as follows (expressed in thousands):

<u>For the Year(s) Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2020	\$ 435	\$ 81	\$ 516
2021	285	63	348
2022	220	52	272
2023	230	43	273
2024	240	34	274
2025-2029	<u>560</u>	<u>42</u>	<u>602</u>
Total	<u>\$1,970</u>	<u>\$315</u>	<u>\$2,285</u>

Changes in long-term debt payable for the year ended June 30, 2019, were as follows (expressed in thousands):

Notes to the Financial Statements (Continued)

	Balance July 1, 2018	Additions	Deletions	Balance June 30, 2019	Amounts Due Within One Year
Revenue bonds payable	\$2,465	\$ -	\$495	\$1,970	\$435
Less: unamortized bond discount	(9)	-	(1)	(8)	-
Add: unamortized bond premium	65	-	25	40	-
Total bonds payable	\$2,521	\$ -	\$519	\$2,002	\$435

Changes in long-term debt payable for the year ended June 30, 2018, are as follows (expressed in thousands):

	Balance July 1, 2017	Additions	Deletions	Balance June 30, 2018	Amounts Due Within One Year
Revenue bonds payable	\$3,050	\$ -	\$585	\$2,465	\$495
Less: unamortized bond discount	(10)	-	(1)	(9)	-
Add: unamortized bond premium	90	-	25	65	-
Total bonds payable	\$3,130	\$ -	\$609	\$2,521	\$495

Events of Default

Debt under the Tennessee Local Development Authority State Loan Program is secured by monthly payments of principal and interest made by local governments in accordance with the loan agreements. Under these loan agreements, local governments agree to levy fees, rates, or charges for services provided by the project and/or ad valorem taxes sufficient to pay debt service requirements. Additional security includes a pledge of state-shared taxes, a debt service reserve, and a statutory reserve.

Upon event of default, the General Bond Resolution empowers the trustee to institute any action or proceedings of law or equity for the collection of all payments due and unpaid under a loan agreement and to require the Authority to withhold state-shared taxes to the extent permitted by law and the terms of the loan agreement. In the event a local government should fail to make a timely and full payment with respect to the loan agreement, the Secretary or Assistant Secretary to the Authority will notify the Commissioner of Finance and Administration (the Commissioner) that the local government has failed to pay loan repayments due and payable with respect to a

Notes to the Financial Statements (Continued)

project and pursuant to the loan agreement and request the Commissioner to notify the local government of the default. The Commissioner shall deliver written notice by certified mail to the local government of such failure within 5 days of such failure. In the event the local government unit fails to remit the required payment or payments within 60 days of receipt of such notice, the Commissioner shall, without further authorization, withhold such sum or part of such sum from the state-shared taxes to make the local government current with respect to the unpaid loan. The balance of any deficit would be secured first by the debt service reserve and then the statutory reserve.

Upon the event of default of principal and interest due on bonds or notes, the Authority shall notify the trustee of such event and the corrective action, if any, the Authority intends to take. Upon the occurrence of an event of default of which the trustee has actual knowledge and at all times thereafter while such default shall continue, the trustee shall become vested with all the estate, property, rights, trusts, duties, and obligations of the trustee and shall take possession or supervision over the funds and account created under the General Bond Resolution and collect and receive all revenues and other monies in the same manner as the Authority and shall act in place of the Authority in the exercise of all rights and duties. The trustee shall give written notice by mail to all the registered holders of the bonds within 60 days after having obtained actual knowledge of default. Upon the occurrence and continuance of an event of default, the trustee: (1) for and on behalf of the holders of the bonds, shall have the same rights which are possessed by the bondholders; (2) shall be authorized to proceed, in its own name and as trustee of an express trust; (3) may pursue any available remedy by action at law or suit in equity to enforce the payment of principal and interest and premium, if any, on the bonds; (4) may file such proofs of claim and other papers or documents as may be necessary; and (5) may, and upon written request of the holders of the bonds of not less than a majority in principal amount of the bonds then outstanding shall proceed to protect and enforce all rights of the bondholders and the trustee as permitted by the General Bond Resolution and the laws of the State of Tennessee.

Note 6. Statutory Reserve

The statutory reserve is an amount set aside in the fund intended to ensure payment of the required annual debt service (principal and interest) for municipalities in the event of a default that have insufficient state-shared taxes available to the Authority to withhold. Per review of the General Bond Resolution, it was determined that this amount should be classified as unrestricted net position. The statutory reserve was funded at \$3 million from appropriations of the state's General Assembly from 1985 to 1987. As of June 30, 2019, the statutory reserve balance was \$3,253,408.

As a part of the application process, each loan applicant pledges its available state-shared taxes, giving the Authority the authorization to intercept these state-shared taxes, should the local government unit fail to repay timely its loan. An analysis is conducted to compare this state-shared tax amount to projected maximum annual debt service. The balance of any deficit would be secured first by the debt service reserve and then the statutory reserve. Of the Authority's current borrowers, Mount Carmel was the only borrower with a deficit. Maximum annual debt service for

Notes to the Financial Statements (Continued)

Mount Carmel is \$130,372. This loan, which is a part of the 2006 Refunding Series A bonds, is scheduled to be paid off in February 2020. The bonds have a final maturity of March 2021.

Note 7. State Infrastructure Fund

The Tennessee Transportation State Infrastructure Fund was created pursuant to Section 4-31-1201, *Tennessee Code Annotated*. The State Infrastructure Program provides assistance to local government units in the construction of transportation infrastructure projects that provide public benefits by enhancing mobility or safety, promoting economic development, or increasing the quality of life and general welfare of the public. In fiscal years 2019 and 2018, no loans were approved.

Note 8. Subsequent Event

On May 28, 2019, S&P Global Ratings placed the Authority's AA+ rating on its outstanding bonds on a credit watch. The placement reflects the decline in the number of participants in the pool as the program has wound down. On October 1, 2019, S&P Global Ratings lowered its rating to AA and removed the rating from the credit watch.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Supplementary Schedules of Net Position - Program Level
June 30, 2019, and June 30, 2018

(Expressed in Thousands)						
	June 30, 2019			June 30, 2018		
	State Loan Programs	State Infrastructure Loan Program	Total	State Loan Programs	State Infrastructure Loan Program	Total
Assets						
Current assets:						
Cash	\$14,217	\$ 825	\$15,042	\$13,584	\$1,142	\$14,726
Receivables:						
Loans receivable	264	57	321	389	-	389
Total current assets	14,481	882	15,363	13,973	1,142	15,115
Noncurrent assets:						
Restricted cash	515	-	515	595	-	595
Loans receivable	1,230	1,433	2,663	1,502	1,126	2,628
Total noncurrent assets	1,745	1,433	3,178	2,097	1,126	3,223
Total assets	16,226	2,315	18,541	16,070	2,268	18,338
Deferred outflows of resources						
Deferred amount on bond refunding	64	-	64	102	-	102
Liabilities						
Current liabilities:						
Accrued interest payable	27	-	27	33	-	33
Payable to borrowers	143	-	143	128	-	128
Revenue bonds payable	435	-	435	495	-	495
Total current liabilities	605	-	605	656	-	656
Noncurrent liabilities:						
Revenue bonds payable, net	1,567	-	1,567	2,026	-	2,026
Total noncurrent liabilities	1,567	-	1,567	2,026	-	2,026
Total liabilities	2,172	-	2,172	2,682	-	2,682
Net position						
Unrestricted	14,118	2,315	16,433	13,490	2,268	15,758
Total net position	\$14,118	\$2,315	\$16,433	\$13,490	\$2,268	\$15,758

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Supplementary Schedules of Revenues, Expenses, and Changes in Net Position - Program Level
For the Years Ended June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	Year Ended June 30, 2019			Year Ended June 30, 2018		
	State Loan Programs	State Infrastructure Loan Program	Total	State Loan Programs	State Infrastructure Loan Program	Total
	Operating revenues					
Revenue from loans	\$ 97	\$ 24	\$ 121	\$ 101	\$ 10	\$ 111
Administrative fees collected	441	2	443	377	1	378
Interest income	322	21	343	183	20	203
Total operating revenues	860	47	907	661	31	692
Operating expenses						
Interest expense	108	-	108	131	-	131
Subsidy to borrowers	13	-	13	13	-	13
Administrative expenses	111	-	111	111	-	111
Total operating expenses	232	-	232	255	-	255
Operating income	628	47	675	406	31	437
Net position						
Net position, July 1	13,490	2,268	15,758	13,084	2,237	15,321
Net position, June 30	\$14,118	\$2,315	\$16,433	\$13,490	\$2,268	\$15,758

TENNESSEE LOCAL DEVELOPMENT AUTHORITY

Supplementary Schedules of Cash Flows - Program Level

For the Years Ended June 30, 2019, and June 30, 2018

	(Expressed in Thousands)					
	Year Ended June 30, 2019			Year Ended June 30, 2018		
	State Loan Programs	State Infrastructure Loan Program	Total	State Loan Programs	State Infrastructure Loan Program	Total
Cash flows from operating activities						
Payments to service providers	\$ (111)	\$ -	\$ (111)	\$ (111)	\$ -	\$ (111)
Net cash used by operating activities	(111)	-	(111)	(111)	-	(111)
Cash flows from noncapital financing activities						
Principal payments	(495)	-	(495)	(585)	-	(585)
Interest paid	(101)	-	(101)	(124)	-	(124)
Net cash used by noncapital financing activities	(596)	-	(596)	(709)	-	(709)
Cash flows from investing activities						
Loans issued	-	(364)	(364)	-	(915)	(915)
Collections of loan principal	400	-	400	464	-	464
Interest received on loans	97	24	121	101	10	111
Administrative revenue	441	2	443	377	1	378
Interest received on pooled investment fund	322	21	343	183	20	203
Net cash provided by (used by) investing activities	1,260	(317)	943	1,125	(884)	241
Net increase (decrease) in cash	553	(317)	236	305	(884)	(579)
Cash, July 1	14,179	1,142	15,321	13,874	2,026	15,900
Cash, June 30	\$14,732	\$ 825	\$15,557	\$14,179	\$1,142	\$15,321
Reconciliation of operating income to net cash used by operating activities:						
Operating income	\$ 628	\$ 47	\$ 675	\$ 406	\$ 31	\$ 437
Adjustments to reconcile operating income to net cash used by operating activities:						
Revenue from loans	(97)	(24)	(121)	(101)	(10)	(111)
Interest income	(322)	(21)	(343)	(183)	(20)	(203)
Interest expense	108	-	108	131	-	131
Subsidy to borrowers	13	-	13	13	-	13
Administrative revenue from borrowers	(441)	(2)	(443)	(377)	(1)	(378)
Total adjustments	(739)	(47)	(786)	(517)	(31)	(548)
Net cash used by operating activities	\$ (111)	\$ -	\$ (111)	\$ (111)	\$ -	\$ (111)



JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

**Independent Auditor’s Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance With *Government Auditing Standards***

The Honorable Bill Lee, Governor
Members of the General Assembly
Members of the Tennessee Local Development Authority

We have audited the financial statements of the Tennessee Local Development Authority, a component unit of the State of Tennessee, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Authority’s basic financial statements, and have issued our report thereon dated January 17, 2020. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Authority’s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Authority’s internal control. Accordingly, we do not express an opinion on the effectiveness of the Authority’s internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be


material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Deborah V. Loveless, CPA, Director
Division of State Audit
January 17, 2020



FINANCIAL AND COMPLIANCE AUDIT REPORT

Clean Water State Revolving Fund

For the Year Ended June 30, 2019

Justin P. Wilson
Comptroller of the Treasury



DIVISION OF STATE AUDIT

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JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

February 13, 2020

The Honorable Bill Lee, Governor
Members of the General Assembly
Members of the Tennessee Local Development Authority
The Honorable David Salyers, Commissioner
Department of Environment and Conservation

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Clean Water State Revolving Fund for the year ended June 30, 2019. You will note from the independent auditor's report that an unmodified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

A handwritten signature in black ink that reads "Deborah V. Loveless".

Deborah V. Loveless, CPA, Director
Division of State Audit

20/012

Audit Report
Clean Water State Revolving Fund
For the Year Ended June 30, 2019

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State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit

Clean Water State Revolving Fund

For the Year Ended June 30, 2019

Opinion on the Financial Statements

The opinion on the financial statements is unmodified.

Audit Findings

The audit report contains no findings.



JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

Independent Auditor's Report

The Honorable Bill Lee, Governor
Members of the General Assembly
Members of the Tennessee Local Development Authority
The Honorable David Salyers, Commissioner
Department of Environment and Conservation

Report on the Financial Statements

We have audited the accompanying financial statements of the Clean Water State Revolving Fund, an enterprise fund of the State of Tennessee, as of and for the years ended June 30, 2019, and June 30, 2018, and the related notes to the financial statements, which collectively comprise the fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to

design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion. Tennessee statutes, in addition to audit responsibilities, entrust certain other responsibilities to the Comptroller of the Treasury. Those responsibilities include serving as a member of the board of directors of the Tennessee Local Development Authority. We do not believe that the Comptroller's service in this capacity affected our ability to conduct an independent audit of the Clean Water State Revolving Fund.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Clean Water State Revolving Fund of the State of Tennessee as of June 30, 2019, and June 30, 2018, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements present only the Clean Water State Revolving Fund, an enterprise fund, and do not purport to, and do not, present fairly the financial position of the State of Tennessee, as of June 30, 2019, and June 30, 2018, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 27, 2019, on our consideration of the Clean Water State Revolving Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the fund's internal control over financial reporting and compliance.



Deborah V. Loveless, CPA, Director
Division of State Audit
November 27, 2019

CLEAN WATER STATE REVOLVING FUND
Statements of Net Position
June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	June 30, 2019	June 30, 2018
Assets		
Current assets:		
Cash (Note 2)	\$ 448,803	\$ 423,883
Loans receivable	36,043	36,059
Total current assets	484,846	459,942
Noncurrent assets:		
Loans receivable	646,924	589,306
Total noncurrent assets	646,924	589,306
Total assets	1,131,770	1,049,248
Liabilities		
Current liabilities:		
Payable to borrowers (Note 3)	173	95
Total current liabilities	173	95
Noncurrent liabilities:		
Customer deposits payable (Note 2)	7,923	7,834
Total noncurrent liabilities	7,923	7,834
Total liabilities	8,096	7,929
Net position		
Unrestricted	1,123,674	1,041,319
Total net position	\$1,123,674	\$1,041,319

The notes to the financial statements are an integral part of this statement.

CLEAN WATER STATE REVOLVING FUND
Statements of Revenues, Expenses, and Changes in Net Position
For the Years Ended June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	Year Ended June 30, 2019	Year Ended June 30, 2018
Operating revenues		
Revenue from loans	\$ 9,442	\$ 9,088
Interest income	9,188	5,451
Total operating revenues	18,630	14,539
Operating expenses		
Administrative expenses	1,035	1,377
Total operating expenses	1,035	1,377
Operating income	17,595	13,162
Nonoperating revenues		
Capitalization grant	18,750	43,030
Total nonoperating revenues	18,750	43,030
Nonoperating expenses		
Principal forgiveness (Note 5)	1,487	2,199
Total nonoperating expenses	1,487	2,199
Income before transfers	34,858	53,993
Transfers in (Note 4)	47,497	1,802
Change in net position	82,355	55,795
Net position, July 1	1,041,319	985,524
Net position, June 30	\$1,123,674	\$1,041,319

The notes to the financial statements are an integral part of this statement.

CLEAN WATER STATE REVOLVING FUND
Statements of Cash Flows
For the Years Ended June 30, 2019, and June 30, 2018

(Expressed in Thousands)

	Year Ended June 30, 2019	Year Ended June 30, 2018
Cash flows from operating activities		
Payments for interfund services	\$ (1,035)	\$ (1,377)
Net cash used by operating activities	(1,035)	(1,377)
Cash flows from noncapital financing activities		
Operating grants received	18,750	43,030
Transfers in	47,497	1,802
Net cash provided by noncapital financing activities	66,247	44,832
Cash flows from investing activities		
Loans issued and other disbursements to borrowers	(95,918)	(101,071)
Collections of loan principal	36,829	32,070
Security deposits from borrowers	283	986
Interest received on loans	9,442	9,088
Interest received on investments	9,361	5,546
Amounts repaid to borrowers	(289)	(57)
Net cash used by investing activities	(40,292)	(53,438)
Net increase (decrease) in cash	24,920	(9,983)
Cash, July 1	423,883	433,866
Cash, June 30	\$448,803	\$423,883
Reconciliation of operating income to net cash used by operating activities:		
Operating income	\$ 17,595	\$ 13,162
Adjustments to reconcile operating income to net cash used by operating activities:		
Revenue from loans	(9,442)	(9,088)
Interest income	(9,188)	(5,451)
Total adjustments	(18,630)	(14,539)
Net cash used by operating activities	\$ (1,035)	\$ (1,377)

The notes to the financial statements are an integral part of this statement.

CLEAN WATER STATE REVOLVING FUND
Notes to the Financial Statements
June 30, 2019, and June 30, 2018

Note 1. Summary of Significant Accounting Policies

Reporting Entity

The Clean Water State Revolving Fund was created to provide local governments and utility districts with low-cost financial assistance to improve and protect water quality and public health. The Clean Water State Revolving Fund has been included in Tennessee's *Comprehensive Annual Financial Report* as an enterprise fund (Sewer Treatment Loan Fund).

Basis of Presentation

The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

Measurement Focus and Basis of Accounting

The accompanying financial statements have been prepared using the accrual basis of accounting and the flow of economic resources measurement focus. Under this method, revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred, regardless of the timing of related cash flows.

Operating revenues and expenses are distinguished from nonoperating items in the Clean Water State Revolving Fund. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with principal ongoing operations. The principal operation of the fund is to provide loans to local governments through a revolving loan fund established under Title VI of the Clean Water Act. Therefore, the principal operating revenues of the fund are from interest on loans made to borrowers. The fund also recognizes interest income as operating revenue. The fund's operating expenses are its administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Cash

This classification includes cash on hand and deposits in the State Pooled Investment Fund administered by the State Treasurer.

Note 2. Deposits

At June 30, 2019, the Clean Water State Revolving Fund had \$440,879,722 in the State Pooled Investment Fund for operating cash purposes, and \$7,923,221 in customer security deposits in the Local Government Investment Pool. At June 30, 2018, the fund had \$416,047,938 in the State Pooled Investment Fund, and \$7,834,578 in the Local Government Investment Pool. The Local

Notes to the Financial Statements (Continued)

Government Investment Pool is part of the pooled investment fund administered by the State Treasurer. The pooled investment fund is authorized by statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The funds are very liquid; there are no minimum amounts or lengths of time for investment. The fund is not rated by a nationally recognized statistical rating organization. The fund's investments are measured at amortized cost. Its investment policy and required risk disclosures are presented in the *State of Tennessee's Treasurer's Report*. That report is posted on the state's website at <http://treasury.tn.gov/>.

Note 3. Payable to Borrowers

This account represents loan principal overpayments that will be refunded to borrowers and interest earned on security deposits, which is due to the borrowers per the loan agreements.

Note 4. Interfund Transfers

Each year since the Clean Water State Revolving Fund Loan Program's inception in 1987, the state has been awarded a capitalization grant from the U.S. Environmental Protection Agency to fund the program. To provide a state match for the federal grant to operate the program, the Clean Water State Revolving Fund received an interfund transfer of \$4,687,400 from the state's general fund during the year ended June 30, 2019, and \$1,802,361 during the year ended June 30, 2018.

In fiscal year ending June 30, 2019, \$42,809,917 was transferred from the Drinking Water State Revolving Fund to the Clean Water State Revolving Fund. The authority for this transfer is provided for in Title 40, *Code of Federal Regulations*, Part 35, Section 3135(e)(4).

Note 5. Principal Forgiveness

In fiscal year 2010, the Clean Water State Revolving Fund received money from the American Recovery and Reinvestment Act (ARRA) of 2009. As part of the conditions stipulated by the Act for acceptance of this money, the State Revolving Fund program granted principal forgiveness to the borrowers. Each community that received an ARRA loan was granted 40% principal forgiveness; thus, only 60% of the total award was recorded as a repayable loan. Additionally, each community was limited to one ARRA loan in an amount that could not exceed \$12.5 million.

Beginning in fiscal year 2011, and continuing through the present, the capitalization grant that the Clean Water State Revolving Fund received also stipulated that the state must subsidize a portion of the borrower loans. Therefore, for the first time as a part of its normal operations, the fund began granting principal forgiveness as a part of the loans made from the capitalization grant. The communities to receive this subsidization are determined according to normal procedures of priority ranking used in the past to make loans. Principal forgiveness is recognized on the statements of cash flows as part of "loans issued and other disbursements to borrowers."



JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

**Independent Auditor's Report on Internal Control Over
Financial Reporting and on Compliance and Other Matters
Based on an Audit of Financial Statements Performed in
Accordance With *Government Auditing Standards***

The Honorable Bill Lee, Governor
Members of the General Assembly
Members of the Tennessee Local Development Authority
The Honorable David Salyers, Commissioner
Department of Environment and Conservation

We have audited the financial statements of the Clean Water State Revolving Fund, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the fund's basic financial statements, and have issued our report thereon dated November 27, 2019. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Clean Water State Revolving Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the fund's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Purpose of This Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.



Deborah V. Loveless, CPA, Director
Division of State Audit
November 27, 2019



JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

Fiscal Year Ending June 30, 2019

TLDA Programs

1. State Loan Program Fund: (Water/Sewer)
 - 5 borrowers
 - 7 loans outstanding
 - \$1,970,000 bonds outstanding (Final maturity 2029)

2. State Infrastructure Fund (Transportation)
 - 1 borrower
 - Disbursements: \$364,001

Operating Income: \$674,295

Net Position at June 30, 2019: \$16,433,367

No new loans are being issued for these programs.

State Revolving Fund Loan Programs

1. Clean Water Fund
 - Disbursements
 - \$95,917,859
 - Collections
 - \$36,829,115 loan principal
 - \$9,441,786 interest
 - Net position at June 30, 2019: \$1,123,673,792

2. Drinking Water Fund
 - Disbursements
 - \$9,547,746
 - Collections
 - \$9,545,135 loan principal
 - \$1,874,506 interest
 - Net position at June 30, 2019: \$187,138,369

No significant changes to accounting and reporting standards.

SRF Program Summary for TLDA June 25, 2020 Audit Committee Meeting

1. Clean Water State Revolving Fund – Financial and Compliance Audit Report (June 30, 2019)

- The audit resulted in no observations or findings

2. EPA Region 4 SRF Program Evaluation Report - Clean Water SRF (CWSRF) Program

- EPA conducted a review of the CWSRF Program December 2-4, 2019
- Items identified by EPA that require action are summarized below with a current status:

#	Item	Action Needed	Status
1	Add American Iron and Steel to CWSRF inspection checklist	Add appropriate language	SRF has included American Iron and Steel to the construction inspection checklist
2	Continue to ensure borrowers follow DBE affirmative steps	Ensure borrowers follow the six affirmative steps to maximize DBE participation	SRF loan documents have been revised to include the six DBE affirmative steps; SRF reviews borrowers’ submittals to ensure compliance; and ensures borrowers have made a good faith effort to incorporate DBE participation

3. EPA Region 4 SRF Program Evaluation Report - Drinking Water SRF (DWSRF) Program

- EPA conducted a review of the DWSRF Program December 2-4, 2019
- Items identified by EPA that require action are summarized below with a current status:

#	Item	Action Needed	Status
1	Increase DWSRF pace (cumulative amount of loans issued as a percentage of loan funds available); TN is currently at 90% and the national average is 96%	Increase number of loans awarded by increasing demand through education, outreach, technical assistance, and other actions	Currently, SRF is receiving marketing assistance from EPA; continuing to increase community engagement; improved PRL solicitation method with greater response in PRLs; improved internal communication and monitoring of PRLs; developed a strategy for small and disadvantaged communities
2	Add American Iron and Steel to DWSRF inspection checklist	Add appropriate language	SRF has included American Iron and Steel to the construction inspection checklist

3	Continue to ensure borrowers follow DBE affirmative steps	Ensure borrowers follow the six affirmative steps to maximize DBE participation	SRF loan documents have been revised to include the six DBE affirmative steps; SRF reviews borrowers' submittals to ensure compliance; and ensures borrowers have made a good faith effort to incorporate DBE participation
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TN Dept. of Env. & Conservation

JAN 29 2020

Division of Water Resources

PROGRAM EVALUATION REPORT

Tennessee
Clean Water State Revolving Fund
Fiscal Year 2019 Program Review

Region 4
U. S. Environmental Protection Agency
December 2019

EXECUTIVE SUMMARY

This report reviews the performance of the Tennessee Department of Environment and Conservation's (TDEC) Clean Water State Revolving Fund program (CWSRF) for the Fiscal Year (FY) 2019. The U. S. Environmental Protection Agency (EPA) is required by 40 CFR§35.3165 to annually assess the success of the state's performance of activities identified in the FY18 CWSRF Intended Use Plan (IUP) and annual report to determine compliance with the terms of the capitalization grant agreement.

During FY19 the state entered into 16 new loans totaling \$83.3 million. The loans provided financing for the planning, design, and construction of wastewater and storm water management facilities. Program pace is a CWSRF metric. It is the percentage of the cumulative amount of loans issued as a percentage of all funds available. The national average for pace of the program is 99 percent. As of June 30, 2019, the reported pace of the program was 95 percent.

The Tennessee CWSRF was found to be administered in accordance with Title VI of the Clean Water Act (CWA) as amended. The program is following all terms, schedules, provisions/assurances of the IUP, the operating agreement between the state and the EPA and the conditions of the Capitalization Grant Agreement.

SECTION I: PURPOSE AND SCOPE

The EPA conducted the FY19 annual review of the Tennessee CWSRF on December 2-4, 2019. The process was conducted as prescribed in Section 606(e) of the CWA, 40 CFR§35.3165, Chapter 7 of the State Revolving Fund Management Manual and the annual review Guidance issued in May 2019. Activities incorporated into the annual review included an analysis of TDEC's 2019 annual report and an on-site visit to the state offices in Nashville, Tennessee.

The annual review included the state's capitalization grant (plus any amendment thereto), the IUP, operating agreement and any additional documentation used to establish or manage the CWSRF in FY19. The scope of the annual review includes consideration of the legal, technical, managerial, financial and operational capabilities of TDEC. Focus areas of review included, but were not limited to, compliance with grant conditions, certifications and assurances, adherence to specific proposals and progress toward stated goals and objectives.

In attendance at the entrance conference for TDEC were Leslie Gillespie-Marthaler, Vena Jones, Jenny Dodd, Andrea Fenwick, Lawanda Johnson, Berih Awala, Felecia Freeman, Alicia West and Derek Martin. Attending from the EPA Region 4 were Sheryl Parsons, Tom Cooney, and Johnnie Purify.

The EPA review team interviewed the identified TDEC staff persons for the following areas: project loan files, loan agreements, standard operating procedures, loan payment records, Disadvantaged Business Enterprises (DBE) records, financial records and any additional documents the state uses to manage the program.

At the completion of the review, an exit briefing was held to review the observations made by the EPA to obtain clarification of any outstanding issues. Attending the exit conference for TDEC were Leslie Gillespie-Marthaler, Vena Jones, Berih Awala, Felecia Freeman, Paula Mitchell, Vince Hayman, and Lawanda Johnson. Attending from the EPA Region 4 were Sheryl Parsons, Tom Cooney and Johnnie Purify.

SECTION II: COMPLIANCE REQUIREMENTS

TDEC's last financial and compliance audit for the year ending June 30, 2019 contained no findings.

The state's DBE program goal for FY19 was 7.8 percent. The state ensures borrowers follow the six affirmative steps for DBE participation. The actual DBE procurement awarded was 5.63 percent.

TDEC is in compliance with the 16 items outlined in the grant agreement. Based on the review, the following items describe the activities and observations of interest:

1. Acceptance of Grant: Payments, 40 CFR§35.3135(a). "The State is required to accept grant payments in accordance with the negotiated payment schedule."

Status: During the reporting period, the state accepted grant payments in accordance with the negotiated payment schedule.

2. State Match, 40 CFR§35.3135(b). “The State is required to deposit into its CWSRF an amount equaling at least 20 percent of the amount of each grant payment. The State match must be deposited on or before the date on which the State receives each payment from the grant award.”

Status: The FY18 capitalization was \$23,316,000. The 20 percent state match amount of \$4,663,200 was provided through state funds.

3. Binding Commitments, 40 CFR§35.3135(c). “The State is required to make binding commitments in an amount equal to 120 percent of each quarterly grant payment within one year after receipt of each quarterly grant payment.”

Status: The state entered into 16 new loans with local governments totaling \$83.3 million in FY19. The state met this requirement.

4. Timely Expenditure of Funds, 40 CFR§35.3135(d). “The State must expend all funds in the CWSRF in an expeditious and timely manner.”

Status: Pace of the program is a CWSRF metric. The overall pace percentage (the cumulative amount of loans issued as a percentage of all funds available) for the state is 95 percent (the national average is 99 percent). The state disbursed a total of \$21,390,743 from the CWSRF in FY19.

5. Eligible Activities, 40 CFR§35.3115, 3120 and 3125. “The CWSRF must be used solely to provide loans and other authorized forms of assistance: (a) to municipalities, inter-municipal, interstate, or state agencies for the construction of publicly owned treatment works as defined in Section 212 of the Act and that appear on the state’s priority list developed pursuant to Section 216 of the Act; and (b) for implementation of a nonpoint source pollution control management program under Section 319 of the Act; and (c) for development and implementation of an estuary conservation and management plan under Section 320 of the Act.”

Status: The state funded wastewater and stormwater projects.

6. Abide by State Law, 40 CFR§35.3135(g). “The State is required to commit or expend each quarterly capitalization grant payment in accordance with the State’s own laws and procedures regarding the commitment or expenditure of revenues.”

Status: In the annual report the state has certified that they followed their own laws and procedures regarding the commitment or expenditure of revenues.

7. Other Federal Authorities, 40 CFR§35.3145(a) “The State is required to comply and to require all recipients of funds directly made available by capitalization grants to comply with applicable federal authorities.”

Status: In the Annual Report, under the provisions of the operating agreement/conditions of their grant, the state certified compliance with other federal authorities.

8. Rules of Cash Draw, 40 CFR§35.3155(d) and §35.3160. “The State may draw cash when the SRF receives a request from the loan recipient, based on incurred costs”

Status: Cash draws for the reporting period ending June 30, 2019 were made in accordance with 40 CFR§35.3160. No improper payments were identified.

9. Generally Accepted Accounting Principles, 40 CFR§35.3135(h). “The State is required to establish fiscal control and accounting procedures that are sufficient to assure proper accounting for payments received by the CWSRF, disbursements made by the CWSRF, and CWSRF balances at the beginning and end of the accounting period. The State must also agree to use accounting, audit and fiscal procedures conforming to generally accepted government accounting standards as these are promulgated by the Governmental Accounting Standard Board.”

Status: In the annual report, the state certified adherence to state auditing and accounting procedures, which comply with the Single Audit Act of 1984 and OMB circular A-128 by reference to the Operating Agreement.

10. Recipient Accounting, 40 CFR§35.3135(i). “The State must agree to require recipients of CWSRF assistance to maintain project accounts in accordance with generally accepted government accounting standards as these are promulgated by the Government Accounting Standards Board.”

Status: The state has complied with this requirement via a condition in the loan agreement for borrowers.

11. Annual Report, 40 CFR§35.3135(j) and §35.3165. “The State must agree to make available an Annual Report to the Regional Administrator on the actual use of the funds, in accordance with Section 606(d) of the CWA.”

Status: The annual report for Tennessee’s CWSRF program was received by September 30, 2019, for the state fiscal year ending June 30, 2019. The report contained adequate and accurate information regarding program implementation.

12. Environmental Reviews, 40 CFR§35.3140. “The State is required to conduct reviews of the potential environmental impacts of all Section 212 construction projects receiving assistance from the CWSRF, including nonpoint source pollution control Section 319 and estuary protection Section 320 projects that are also Section 212 projects. The State may elect to apply the procedures at 40 CFR Part 6, subpart E and related subparts, or apply its NEPA like SERP for conducting environmental reviews.”

Status: The state has a NEPA-like SERP which was approved by the Region 4 Regional Administrator. Two projects were reviewed for compliance with the SERP. Both reviewed projects followed the SERP and were well documented.

13. Consistency with Planning, 40 CFR§35.3125(e). “The CWSRF may provide assistance only to projects that are consistent with any plans developed under Sections 205(j), 208, 303(e), 319 and 320 of the CWA.”

Status: The state is in compliance with this regulation, funding eligible wastewater and stormwater projects.

14. Outlay Management, 40 CFR§35.3155(b). “With the application for a capitalization grant, the State shall submit a schedule that reflects, by quarters, the estimated disbursements from that grant for the year following the grant award date. This schedule must be developed in conformity with the procedures applicable to cash draws in 40 CFR§35.3160 and must be sufficient to allow the Agency and the State to jointly develop and maintain a forecast of cash draws.”

Status: The state complied with this regulation in the IUP.

15. Intended Use Plan, 40 CFR§35.3150. “The State must prepare a plan identifying the intended uses of the funds in the CWSRF and describing how those uses support the goals of the CWSRF. The IUP must be prepared annually and must be subjected to public comment and review before being submitted to the EPA. The EPA must receive the IUP prior to the award of the capitalization grant. According to Section 606(c) of the CWA, after providing the IUP for public comment and review, each State shall annually prepare a plan identifying the intended uses of the amounts (including repayments) available to its water pollution control revolving fund.”

Status: The state’s FY19 IUP was complete and included repayments and interest earnings in the amounts available for assistance.

16. Perpetuity, 40 CFR§35.3100(a). “Section 606(c) requires that the States shall annually prepare a plan identifying the intended uses of the amounts available to its water pollution control revolving fund. Generally, based on an Office of General Counsel opinion in a January 19, 1995, a one-year time frame seems reasonable for committing repayments and other funds to projects. If all available funds are not committed to projects, then the IUP must contain a plan which details how and when the funds will be used.”

Status: The state is complying with this requirement. The state has a plan to commit funds to projects in a timely fashion.

SECTION III: PROGRAM GOALS

TDEC has two long term goals and two short term goals in their FY18 IUP. Status is directly cited from TDEC’s CWSRF annual report. The goals and accomplishments reviewed for the FY19 Program Evaluation Report, include:

Long term goal and status:

1. Provide local governments with low cost financial assistance.

Status: Fiscal responsibilities are coordinated with TDEC, the Comptroller's Office and the Department of Finance and Administration. TDEC is pursuing a new data base for tracking projects and has introduced an improved ability to pay index to help make interest rate and subsidy decisions.

Short term goal and status:

2. Manage an effective and efficient CWSRF loan program.

Status: In FY19, TDEC developed new Standard Operation Procedures (SOP) for technical and financial review process for projects and developed a streamlined contacts database for outreach.

SECTION IV: PROJECT FILES REVIEWED

Two project files were reviewed during the annual oversight review. These projects were:

Goodlettsville, a \$4,200,000 20-year loan for sewer collection system rehabilitation. The loan was awarded on July 17, 2018. The interest rate was 1.9 percent. A Categorical Exclusion was issued on June 12, 2018.

Hamilton County, a \$2,474,000 20-year loan for sewer collection system rehabilitation. The loan was awarded November 26, 2018. The interest rate was 2.35 percent. A Categorical Exclusion was issued on October 10, 2018.

Both projects were eligible for SRF funding and followed all environmental review and procurement requirements.

SECTION V: ENVIRONMENTAL BENEFITS REPORTING

During FY19, the state entered into 16 new loans totaling \$83.3 million with local governments.

TDEC updated the Clean Water Benefits Reporting (CBR) database as required by the grant agreement in a timely fashion. All necessary information about projects funded in FY19 was entered into the CBR system.

SECTION VI: CASH DRAWS

Draws were reviewed during the annual oversight visit. The draws were: \$349,487.69 on June 20, 2019; \$1,696,375.47 on June 24, 2019; \$318,893.91 on June 27, 2019 and \$115,050.83 on March 13, 2019. No improper payments were identified.

SECTION VII: FINANCIAL INDICATORS

Return on federal investment is a performance measure used to evaluate the efficiency of an investment, that is, it measures gain (or loss) generated relative to the federal dollars invested. The state's return on federal investment is 231 percent compared with the national average of 284 percent. (Figure 1)

The national average for the pace of the program in the CWSRF is 99 percent. As of June 30, 2019, the pace of the CWSRF was 95 percent. (Figure 2)

Disbursements as a percentage of assistance provided shows how quickly loans are being disbursed to borrowers, which follows costs incurred. TDEC's disbursement percentage is 81 percent compared to the national average of 88 percent. (Figure 3)

Uncommitted balances are the amount of funds the state has available for loans that are not committed to loans. Tennessee's uncommitted balance for FY19 is \$101.7 million, with a ratio of 1.20 percent. (Figure 4)

On the basis of our financial review, we conclude the TDEC CWSRF is in sound financial condition.

SECTION VIII: FOLLOW UP ON PRIOR YEAR PROGRAM EVALUATION REPORT RECOMMENDATIONS

The following items were the EPA recommendations for the TDEC CWSRF program in the FY18 CWSRF Program Evaluation Report:

1. It is recommended the state finalize their updated draft operating agreement to reflect the Water Resource Reform and Development Act amendment changes as well as changes in their program.

Status: The state provided a draft operating agreement on December 30, 2019. The state has also been proactive in updating their SOP.

2. It is recommended the state add American Iron and Steel and Davis-Bacon to their inspection checklist.

Status: The state has developed a greatly improved checklist that does include Davis-Bacon. American Iron and Steel has not been added.

3. It is recommended the state update loan agreements to include the most current American Iron and Steel and Davis Bacon provisions.

Status: The state has completed this recommendation.

4. It is recommended the state consider increasing the amount of the loan closing fee charged.

Status: The state is continuing to work with the Comptroller's Office and fiscal services to consider fee increases and long-term objectives of the program.

SECTION IX: RECOMMENDATIONS

1. It is recommended that the state add American Iron and Steel to the inspection checklist.
2. It is recommended that the state continue to follow the six affirmative steps and try to increase DBE participation.

APPENDIX: CWSRF Program Financial Indicators

Figure 1 - TN CWSRF - Return on Federal Investment

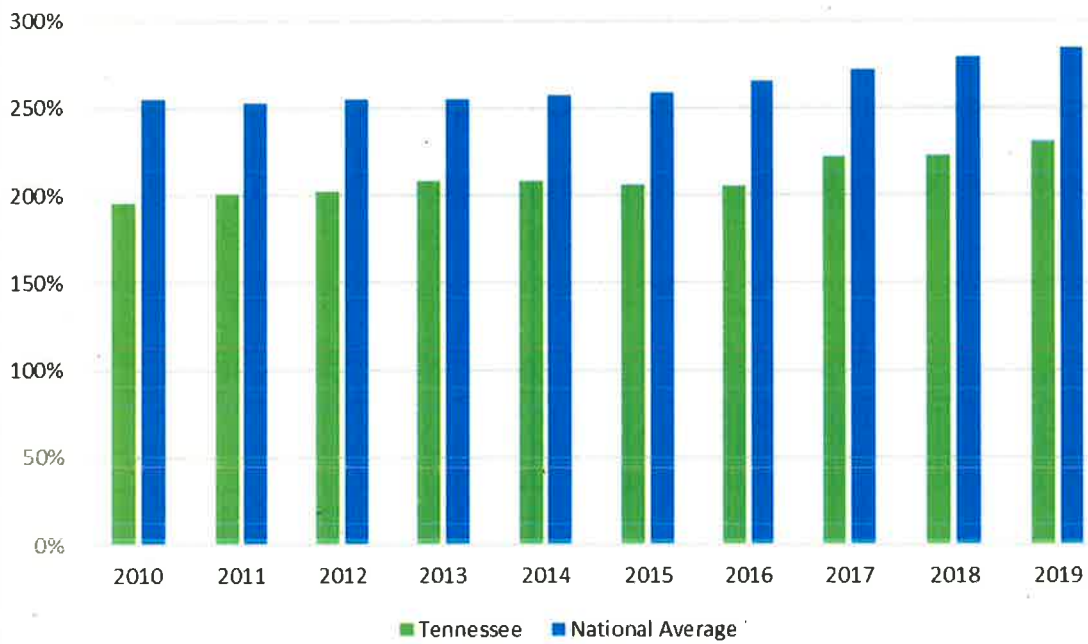


Figure 2 - TN CWSRF - Assistance Provided as a % of Funds Available (Program Pace)

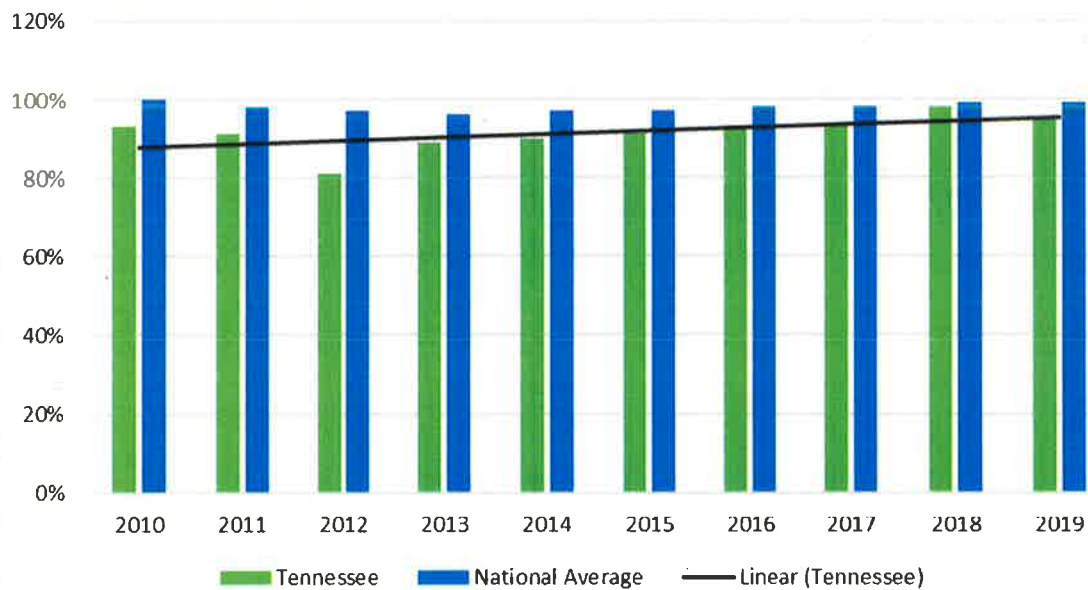


Figure 3 - TN CWSRF - Disbursements as a % of Assistance Provided

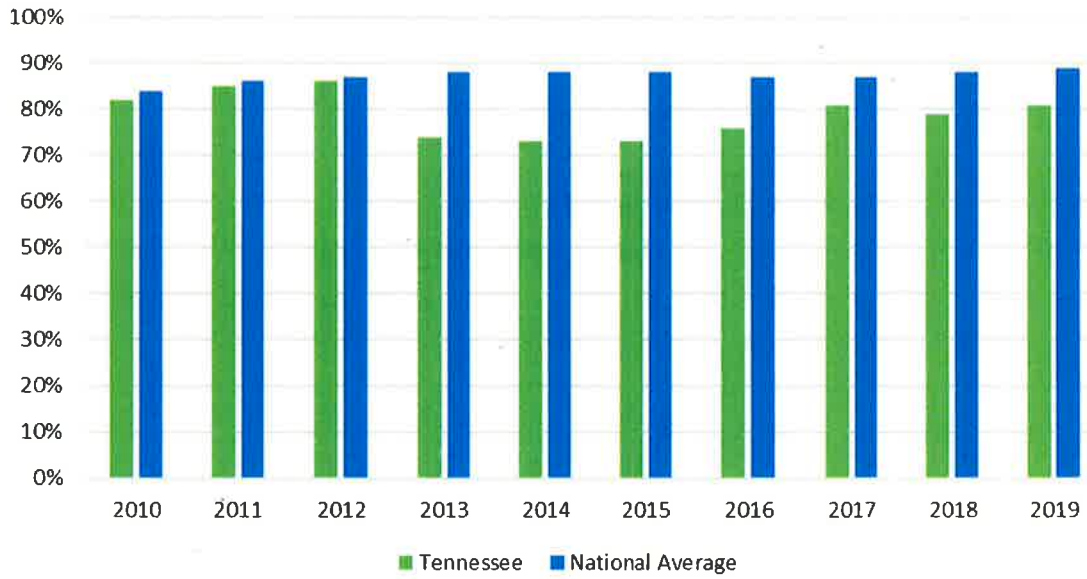
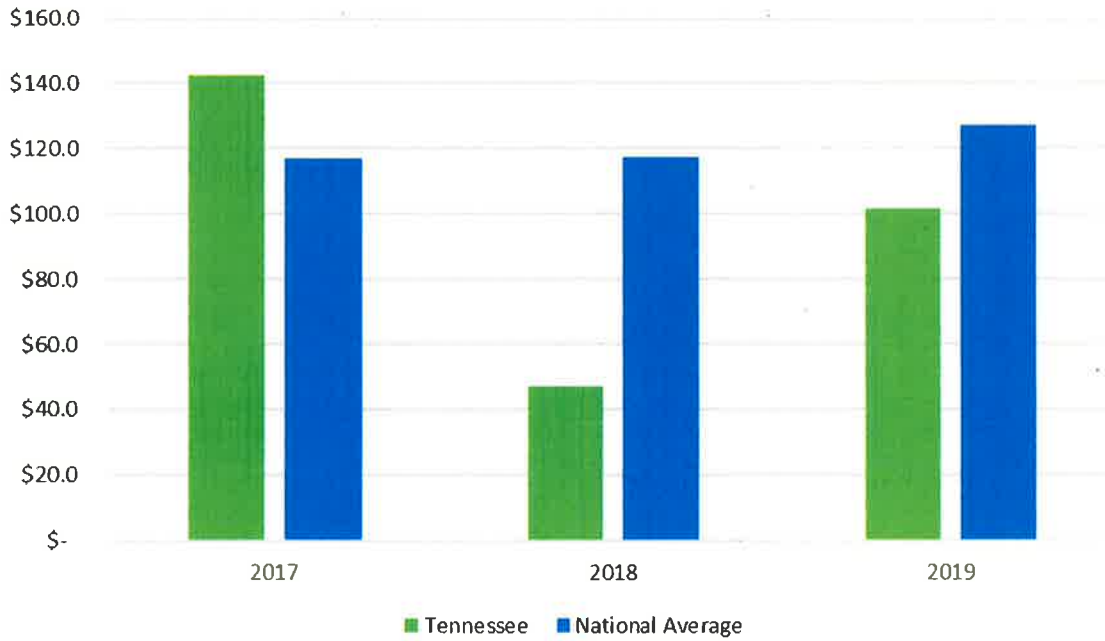


Figure 4 - TN CWSRF - Uncommitted Balances (\$ Millions)



PROGRAM EVALUATION REPORT

Tennessee
Drinking Water State Revolving Fund
Fiscal Year 2019 Program Review

Region 4
U. S. Environmental Protection Agency
December 2019

EXECUTIVE SUMMARY

This Program Evaluation Report (PER) reviews the performance of the Tennessee Department of Environment and Conservation's (TDEC) Drinking Water State Revolving Fund program (DWSRF) for the Fiscal Year (FY) 2019. The U. S. Environmental Protection Agency (EPA) is required by 40 CFR§35.3570 to annually assess the success of the state's performance of activities identified in the FY18 DWSRF Intended Use Plan (IUP) and FY19 annual report to determine compliance with the terms of the capitalization grant agreement.

During FY19, the state entered into eight loans totaling \$13,345,300 with local governments for the construction of drinking water facilities. Pace is a DWSRF program metric. It is the percentage of the cumulative amount of loans issued as a percentage of all funds available. The national average for the pace of the program is 96 percent. As of June 30, 2019, the reported pace of the program was 90 percent.

The Tennessee DWSRF has been administered in accordance with Section 1452 of the SDWA as amended, and is in compliance with the terms, schedules, provisions and assurances of the current FY IUP, work plans, the current operating agreement between the state and the EPA and the conditions of the DWSRF Capitalization Grant Agreements.

SECTION I: PURPOSE AND SCOPE

The EPA Region 4 conducted the FY19 annual review of Tennessee DWSRF on December 2-4, 2019. The process was conducted as prescribed in Section 1452 of the Safe Drinking Water Act, 40 CFR§35.3575 and in the Annual Review Guidance issued May 2019. Activities incorporated into the annual review included an analysis of Tennessee's 2019 annual report and an onsite visit to the state offices in Nashville, Tennessee.

The annual review included the state's Capitalization Grant (plus any amendment thereto), the IUP, operating agreement and any additional documentation used to establish or manage the DWSRF during FY19. The scope of the annual review includes consideration of the legal, technical, managerial, financial and operational capabilities of TDEC. Focus areas of review included, but were not limited to, compliance with grant conditions, certifications and assurances, adherence to specific proposals, progress toward stated goals and objectives.

In attendance at the entrance conference for TDEC were Leslie Gillespie-Marthaler, Vena Jones, Jenny Dodd, Andrea Fenwick, Lawanda Johnson, Berih Awala, Felecia Freeman, Alicia West and Derek Martin. Attending from the EPA Region 4 were Sheryl Parsons, Tom Cooney, and Johnnie Purify.

The EPA review team interviewed the appropriate staff persons as identified at the entrance conference and reviewed the following: project loan files, loan agreements, standard operating procedures, loan payment records, Disadvantaged Business Enterprises (DBE) records, financial records and any other documents the state uses to manage the program.

At the completion of the review, an exit briefing was held to review the observations made by the EPA to obtain clarification of any outstanding issues. Attending the exit conference for TDEC were Leslie Gillespie-Marthaler, Vena Jones, Berih Awala, Felecia Freeman, Paula Mitchell, Vince Hayman, and Lawanda Johnson. Attending from the EPA Region 4 were Sheryl Parsons, Tom Cooney and Johnnie Purify.

SECTION II: COMPLIANCE REQUIREMENTS

TDEC's last financial and compliance audit for the year ending June 30, 2019 contained no findings.

The state's DBE program goal for FY19 was 7.8 percent. The state ensures borrowers follow the six affirmative steps for DBE participation. The actual DBE procurement awarded was 2.67 percent.

TDEC is in compliance with the 13 assurances stated in the grant agreement, including capacity development and operator certification requirements. These assurances have their basis in 40 CFR§35.3550.

Based on the review, the following items describe the activities and observations of interest:

1. Assurance that the state has the authority to establish a fund and to operate the DWSRF program in accordance with the SDWA.

Status: The state provided the required Attorney General certification with the grant application.

2. Assurance that the state will comply with state statutes and regulations and abide by state law.

Status: The state certified this in the FY18 IUP.

3. Assurance that the state has the technical capability to operate the program.

Status: The state is in compliance with this assurance.

4. Assurance that the state will accept capitalization grant funds in accordance with a payment schedule.

Status: The state certified this in the FY18 IUP.

5. Assurance that the state will deposit all capitalization grant funds in the fund or set-aside account.

Status: The state has deposited the capitalization grant appropriately.

6. Assurance that the state will provide an amount at least equal to 20 percent of the capitalization grant (state match) in the fund.

Status: The FY18 capitalization grant was \$19,293,000. The 20 percent state match amount of \$3,858,600 was provided through state funds.

7. Assurance that the state will deposit net bond proceeds, interest earnings and repayments into the fund.

Status: The state does not leverage. All repayments and interest earnings are credited to the fund.

8. Assurance that the state will use Generally Accepted Accounting Principles.

Status: As noted in the FY19 state audit, the state has complied with this assurance.

9. Assurance that the state will have the fund and set-aside account audited annually in accordance with Generally Accepted Government Auditing Standards.

Status: The DWSRF is audited with the state accounts.

10. Assurance that the state will adopt policies and procedures to assure that borrowers have a dedicated source of revenue for repayments (or in the case of a privately-owned system, demonstrate that there is adequate security).

Status: The state has complied with this assurance in loan agreements to borrowers.

11. Assurance that the state will commit and expend funds as efficiently as possible and in an expeditious and timely manner.

Status: The overall pace percentage for the state is 90 percent which increased by three percent from FY18 (the national average is 96 percent). The state disbursed a total of \$2,368,758 from the DWSRF in FY19.

12. Assurance that funds will be used in accordance with the IUP.

Status: The annual report documents the state is in compliance with this assurance.

13. Assurance that the state will provide the EPA with a Biennial Report.

Status: TDEC has elected to provide an annual report to the EPA. The annual report for Tennessee's DWSRF program was received by September 30, 2019, for the state FY ending June 30, 2019. The report contained adequate and accurate information.

SECTION III: PROGRAM GOALS

TDEC has two long term goals and two short term goals in their IUP. Status is directly cited from TDEC's DWSRF annual report. The goals and accomplishments reviewed for the FY19 Program Evaluation Report, include:

Long term goal and status:

1. Provide local governments with low cost financial assistance.

Status: Fiscal responsibilities are coordinated with TDEC, the Comptroller's Office and the Department of Finance and Administration. TDEC is pursuing a new data base for tracking projects and has introduced an improved ability to pay index to help make interest rate and subsidy decisions.

Short term goal and status:

2. Manage an effective and efficient CWSRF loan program.

Status: In FY19, TDEC developed new Standard Operation Procedures (SOP) for technical and

financial review process for projects and developed a streamlined contacts database for outreach.

SECTION IV: PROJECT FILES REVIEWED

There were two project files reviewed during the annual oversight review. The projects were:

Ocoee Utility District, a \$3,799,300 loan for a water storage tank and line replacement. The loan was awarded on November 26, 2018. The interest rate was 1.48 percent. A Categorical Exclusion was issued on September 20, 2018.

Smith Utility District, a \$933,000 loan for construction of a new 300,000-gallon water storage tank and associated appurtenances. The loan was awarded on December 12, 2018. The interest rate was 0.79 percent. A Categorical Exclusion was issued on August 22, 2018.

Both projects were eligible for DWSRF funding and followed the environmental review and procurement requirements.

SECTION V: ENVIRONMENTAL BENEFITS REPORTING

During FY19, the state entered into eight new loans totaling \$13,345,300 to local governments for the construction of drinking facilities.

TDEC updated the Public Water Supply Benefits Reporting (PBR) database as required by the grant agreement in a timely fashion. All necessary information about projects funded in FY19 had been entered in the PBR system.

SECTION VI: CASH DRAWS

Draws were reviewed during the annual oversight visit. The draws were \$6,285.19 on July 2, 2018; \$139.15 on September 11, 2018; \$5.45 on July 19, 2018; \$5.45 on September 13, 2018; \$17.19 on March 12, 2019; \$10.90 on March 11, 2019 and \$129,904.01 on June 3, 2019. No improper payments were identified.

It was noted during the review that the DWSRF program did not review and approve set aside draws. This is an internal control issue. The EPA Region 4 discussed this with TDEC during the review and Tennessee immediately implemented a review and approval process.

SECTION VII: FINANCIAL INDICATORS

Return on federal investment is a performance measure used to evaluate the efficiency of an investment, that is, it measures the gain (or loss) generated relative to the federal dollars invested. The state's return on federal investment is 131 percent. The national average is 200 percent. (Figure 1)

The national average for the pace of the program in the DWSRF is 96 percent. As of June 30, 2019, the pace of the program was 90 percent (cumulative amount of loans issued as a percentage of all funds available). (Figure 2)

Disbursements as a percentage of assistance provided shows how quickly loans are being disbursed to borrowers, which, of course, follows costs incurred. TDEC's disbursement percentage is 102 percent compared to the national average of 88 percent. (Figure 3)

Uncommitted balances are the amount of funds the state has available for loans that are not committed to loans. Tennessee's uncommitted balance for FY19 is \$75.2 million, with a ratio of 4.3 percent. (Figure 4)

On the basis of our financial review, we conclude the TDEC DWSRF is in sound financial condition.

SECTION VIII: SET ASIDE PERFORMANCE

The DWSRF program gives states the option of using up to 31 percent of their capitalization grant for activities that protect sources of drinking water and enhance water systems management. Tennessee has elected to use the set-asides in the following manner:

State Program Management

Section 1452(g) (2) of the SDWA allows up to 10 percent of the DWSRF capitalization grant to be set-aside to support other program initiatives of the SDWA. For State Program Management, the State used \$654,221. These funds provided program support for the PWSS program, including data management and compliance.

Small System Technical Assistance

In FY19, the program used \$309,562 for this set aside. The Fleming Training Center (FTC) in Murfreesboro, Tennessee administers the small system technical assistance set-aside. The FTC conducts operator training for water operators. For FY19, 145 operators were trained, and 314 days of instruction provided.

SECTION IX: FOLLOW UP ON PRIOR YEAR PROGRAM EVALUATION REPORT

The following items were the EPA recommendations for the TDEC DWSRF program in the FY18 DWSRF Program Evaluation Report:

1. It is recommended the state continue efforts to increase the pace of the program.

Status: The state is currently utilizing the services of the EPA contractor to develop marketing plans.

2. It is recommended the state finalize their updated draft Operating Agreement with the EPA Region 4 to incorporate the Water Infrastructure Improvements for the National Act by December 31, 2019.

Status: The state provided a draft operating agreement on December 30, 2019. The state has also been proactive in updating their SOP.

3. It is recommended the state consider increasing the amount of loan fee charged.

Status: The state is continuing to work with the Comptroller's Office and fiscal services to consider fee increases and long-term objectives of the program

4. It is recommended the state continue to ensure borrowers follow the six affirmative steps to maximize DBE participation.

Status: The state continues to take the necessary steps to ensure DBE participation.

SECTION X: RECOMMENDATIONS

1. It is recommended that the state increase the pace of the program. As of June 30, 2019, the pace of the program was 90 percent). The national average for the DWSRF is 96 percent. The state is currently utilizing the services of the EPA contractor to develop marketing plans. The EPA Region 4 will continue to provide technical assistance.
2. It is recommended that the state add American Iron and Steel to the inspection checklist.
3. It is recommended that the state continue to follow the six affirmative steps and try to increase DBE participation.

APPENDIX: DWSRF Program Financial Indicators

Figure 1 - TN DWSRF - Return on Federal Investment

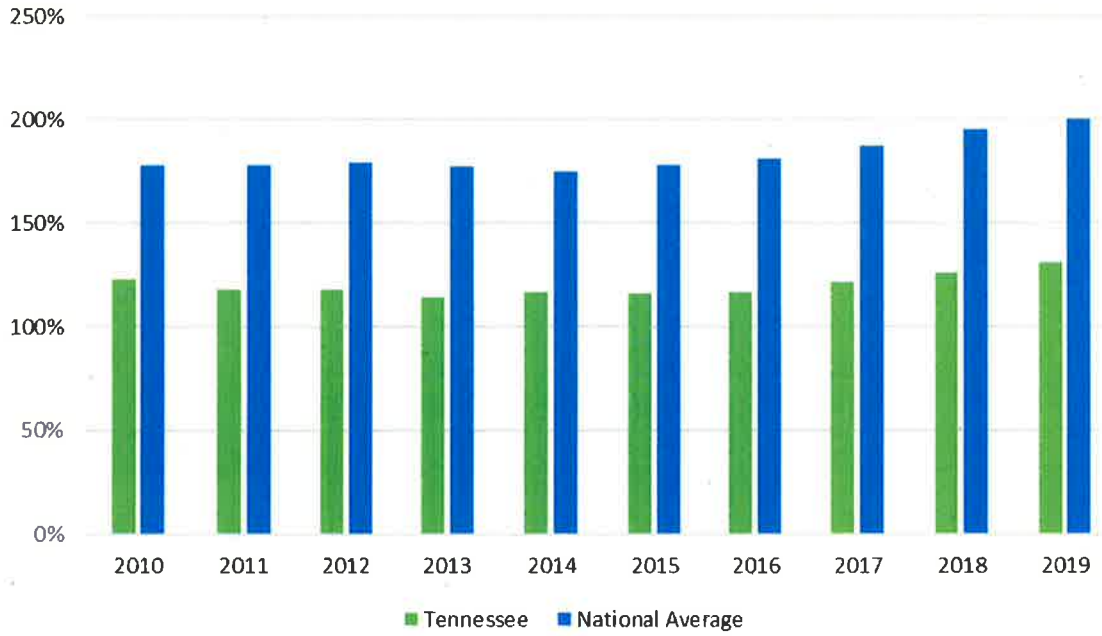


Figure 2 - TN DWSRF - Assistance Provided as a % of Funds Available (Program Pace)

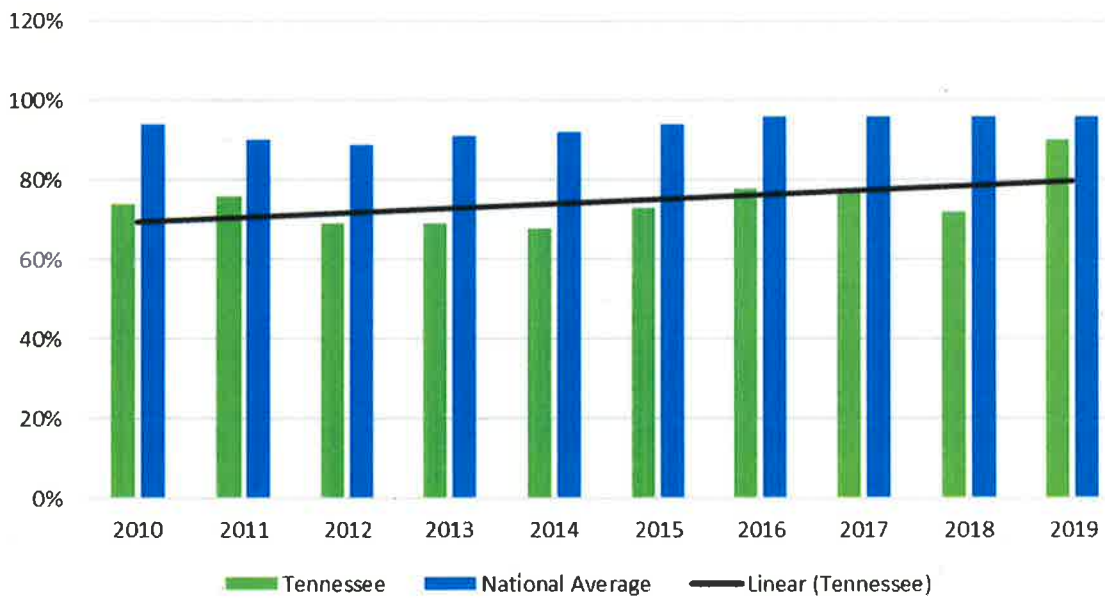


Figure 3 - TN DWSRF - Disbursements as a % of Assistance Provided

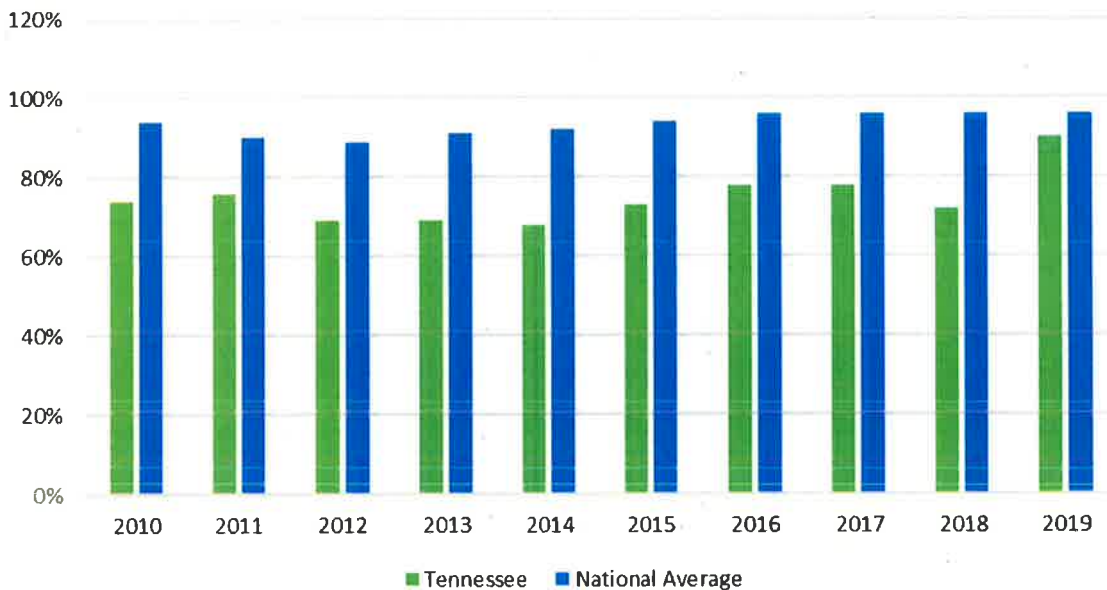
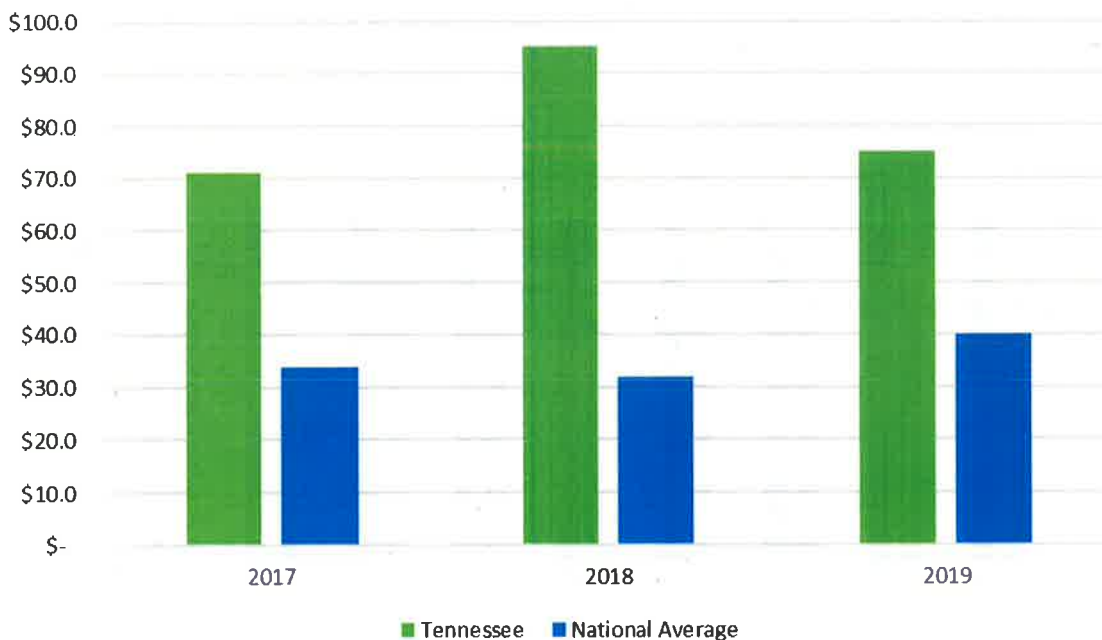


Figure 4 - TN DWSRF - Uncommitted Balances (\$ Millions)





JUSTIN P. WILSON
Comptroller

JASON E. MUMPOWER
Deputy Comptroller

To: Members of the Tennessee Local Development Authority (TLDA) Audit Committee

From: Sandi Thompson, Director, Office of State and Local Finance (OSLF) *Sandi Thompson*

Date: June 15, 2020

Subject: Risk Assessments

The management risk assessments for the OSLF and the Division of Water Resources are attached. These annual reports address agency-wide risk management and internal control requirements of Tenn. Code Ann. § 9-18-102, known as the Tennessee Financial Integrity Act, as amended.

This code requires that each agency of state government and institution of higher education to establish and maintain internal controls, to provide reasonable assurance that:

- (1) Obligations and costs are in compliance with applicable law;
- (2) Funds, property and other assets are safeguarded against waste, loss, unauthorized use or misappropriation; and
- (3) Revenues and expenditures applicable to agency operations are properly recorded and accounted for to permit the preparation of accurate and reliable financial and statistical reports and to maintain accountability over the assets.

To document compliance with the requirements set forth above, the code requires that each agency of state government and institution of higher education annually perform a management assessment of risk and that the internal controls discussed above be incorporated into such assessment.

The objectives of the annual risk assessment are:

- (1) to provide accountability for meeting program objectives;
- (2) to promote operational efficiency and effectiveness;
- (3) to improve reliability of financial statements;
- (4) to strengthen compliance with laws, regulations, rules, and contracts and grant agreements; and
- (5) to reduce the risk of financial or other asset losses due to fraud, waste and abuse.

Fraud Report Affirms Internal Audit's Value at Critical Time

Richard Chambers April 27, 2020 [Comments](#)



Each year, the Association of Certified Fraud Examiners (ACFE) publishes a "Report to the Nations," which shares results of its annual Global Fraud Survey. The findings reflect the significant role that internal audit plays, and the value it adds, in detecting and deterring fraud. Indeed, internal audit consistently ranks second only to whistleblower tips as the most effective way to uncover wrongdoing.

This year's report is no different, except in one very important way: Its message about internal audit's value is needed now more than ever.

In addition to its deeply serious health implications, COVID-19 is part of any and every discussion about business and society. From its dramatic impact on global economic engines and its spawning of a telecommuting revolution, to the growing anxiety brought on by social distancing's isolation, the pandemic dominates every waking hour.

And so it is with occupational fraud. The pandemic is creating conditions where occupational fraud can thrive. Anyone with the slightest understanding of fraud is familiar with the concept of the fraud triangle, which identifies pressure, opportunity, and rationalization as the key ingredients. The pandemic is fueling the first — pressure — in myriad ways, as its impact on economies threatens the financial well-being of millions of organizations and billions of workers globally.

The second, opportunity, could easily expand as organizations scramble to cut costs, even at the expense of effective controls. ACFE President and CEO Bruce Dorris describes the dangers behind this faulty thinking perfectly in the news release announcing the report, *Coronavirus Pandemic Is a Perfect Storm for Fraud*.

"Companies seeking to cut costs often target non-revenue-generating departments like compliance and internal audit. This is a mistake. Cutbacks to departments or initiatives that are integral to a comprehensive anti-fraud program only serve to leave organizations more vulnerable to the growing likelihood of fraud. As organizations make cuts in the attempt to operate with a leaner staff, they can find themselves caught in a perfect storm for fraud: Pressures motivating employee fraud are high at the same time that defenses intended to safeguard against fraud have been weakened."

ACFE is not alone in recognizing the growing threat of fraud and corruption created by the pandemic. The Council of Europe's Group of States Against Corruption (GRECO) has issued a similar warning.

In a report published April 15, GRECO President Marin Mrčela cautioned:

"As countries face undeniable emergencies, concentration of powers, derogations from fundamental rights and freedoms, and as large amounts of money are infused into the economy to alleviate the crisis (now and in the near future), corruption risks should not be underestimated. It is therefore most important that anti-corruption is streamlined in all COVID-19, and more generally, pandemic-related processes."

The ACFE Report to the Nations provides ample evidence of internal audit's critical role in fighting occupational fraud and corruption. Its examination of more than 2,500 fraud cases in 125 countries that occurred in 2019 tells us the following about internal audit:

- Internal audit uncovered the fraud in 15% of cases examined.
- Internal audit (74%) was the third most common control among survey respondents behind external audit (83%) and codes of conduct (81%).
- When internal audit is in place, median losses to occupational fraud were cut in half (\$100,000 vs \$200,000).
- When internal audit is in place, duration of frauds was cut in half (12 months vs. 24 months).

The report also provides significant data that internal auditors can mine to help them detect and deter fraud. This includes data on common methods of fraud, breakdowns on fraud occurrences by organization type, average loss per incident by industry, demographic profiles of fraudsters, common red flags to help identify wrongdoing, and more.

I urge every practitioner to [download](#) a copy of the report. Not only does it provide valuable information to help internal audit ferret out fraud, it also provides ample evidence of internal audit's value for stakeholders.

The COVID-19 pandemic has shined a bright light on how organizations respond to significant crisis, and all evidence suggests that internal audit is playing a significant, relevant, and valuable role. We must continue to do our very best work as we move forward. What's more, we must be vigilant and counsel against short-sighted efforts to save costs by eliminating or weakening effective and proven controls.

As always, I look forward to your comments.