AGENDA

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
AUDIT COMMITTEE
JUNE 23, 2025, 2:20 PM
CORDELL HULL BUILDING, VOLUNTEER CONFERENCE CENTER, 2ND FLOOR

1. Call Meeting to Order
2. Approval of the AC Meeting Minutes July 22, 2024 *
3. Review Audit Reports Issued by Comptroller's Office
    a. Discuss TLDA Audit Report
    b. Discuss Clean Water State Revolving Fund Audit Report
4. Review Financial Statements including Significant Accounting & Reporting Standards
5. SRF Summary of PERS Reports from EPA
    a. 2023 EPA TN PERS Report Cover Letter
    b. 2023 TN_SRF Drinking Water PERS Report
    c. 2023 TN_SRF Clean Water PERS Report
6. Risk Assessments
    a. Risk Assessments Memo
    b. 2024 SGF Risk Assessment
    c. 2024 TDEC Water Resource Risk Assessment
7. Discuss Management's Responsibility to Prevent, Detect & Report Fraud, Waste & Abuse
8. Discuss Comptroller Hotline
9. Audit Committee Responsibilities Calendar
10. Opportunity for Public Comment
11. Other Business
12. Adjournment

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

Agenda Item #2

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
AUDIT COMMITTEE MEETING MINUTES
July 22, 2024

The Tennessee Local Development Authority (TLDA) Audit Committee met on Monday, July 22, 2024. The meeting began at 3:52 p.m. in the Volunteer Conference room of the Cordell Hull Building.

The following members were present:

- David H. Lillard, Jr., State Treasurer
- Mayor Rollen Bradshaw, Loudon County, TN
- Mayor Paige Brown, Gallatin, TN. (By Phone)
- Chris Mustain, Designee for Tre Hargett, Tennessee Secretary of State
- Jim Bryson, F&A Commissioner

Others present were:

- Sandi Thompson, Director, Office of State Government Finance
- Alicia West, Program Accountant, Office of State Government Finance
- Earle Pierce, Director of Internal Audit, TN Department of Treasury
- Paula Mitchell, Deputy Director, TN Department of Environment and Conservation (TDEC)

Call Meeting to Order

Chairman Lillard called the meeting to order with a quorum present.

Approval of Meeting Minutes

Chairman Lillard presented the minutes from the June 15, 2022, TLDA Audit Committee meeting for approval. There were no other recommended changes. Mayor Bradshaw motioned to accept the minutes as presented and Commissioner Bryson seconded the motion. Sandi Thompson called the roll.

Roll Call: Chris Mustain-Aye, Chairman Lillard-Aye, Commissioner Bryson-Aye, Mayor Bradshaw-Aye, Mayor Brown-Aye.

The motion passed unanimously.

Review Audit Reports Issued by Comptroller's Office

Chairman Lillard recognized Tabitha Furlong from State Audit to review the audit reports for the Tennessee Local Development Authority (TLDA) and the Clean Water State Revolving Fund (CWSRF). Ms. Furlong informed the Committee the TLDA and CWSRF received unmodified opinions on their June 30, 2023, financial statements. The audit opinions were issued December 12, 2023, with the reports released to the public on January 12, 2024. No findings were noted.

Agenda Item #2

Review Financial Statements Including Significant Accounting and Reporting Standards

Chairman Lillard recognized Alicia West to review the financial results for the TLDA and the SRF loan programs as of June 30, 2023. Ms. West presented an overview of the financial results noting no changes in any significant accounting or reporting standards.

Program Evaluation Review (PERs) Reports from the EPA

Chairman Lillard recognized Paula Mitchell, Deputy Director from the TN Department of Environment and Conservation to discuss the results of the FY2022 PERS reviews from the EPA. Ms. Mitchell informed the Committee TDEC is waiting on the FY23 PERS results from the EPA. Ms. Mitchell discussed the results of the FY22 PERS results from the EPA. There were no findings with some recommendations for program improvements. Ms. Mitchell discussed the EPA recommendations and the actions taken to address them including making offers to applicants which will help address some of the staffing issues. The state water infrastructure grants program and the state revolving fund program were merged into one program to improve technically expertise and efficiency. TDEC issued a Request For Information (RFI) to obtain information from contractors who can provide a new database to manage their state revolving fund loans. They anticipate a formal Request For Proposal in November 2024 with implementation to take about 12 months. The EPA had similar recommendations for TDEC's drinking water program.

State Government Finance 2023 Risk Assessments

Chairman Lillard recognized Sandi Thompson to discuss the Office of State Government Finance (SGF) and Division of Water Resources 2023 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 & the Comptroller's Hotline

Chairman Lillard recognized Sandi Thompson to speak about management's responsibility to prevent, detect, and report fraud, waste, and abuse. Ms. Thompson spoke about her review of the Comptroller's website for reporting fraud, waste, and abuse. The Comptroller's hotline has been in service since 1983.

Responsibilities Calendar

Chairman Lillard recognized Earle Pierce to discuss the TLDA Audit Committee Responsibilities Calendar. Mr. Pierce reviewed a listing of audit committee responsibilities as outlined in the TLDA Audit Committee charter. He noted the purpose of the calendar was to keep the Committee members apprised of how the Committee met their responsibilities or how others met those responsibilities on behalf of the audit committee over the past year.

Agenda Item #2

Opportunity for Public Comment

No public comments were made.

Other Business

No other business was discussed.

Adjournment

Chairman Lillard motioned to adjourn. Commissioner Bryson seconded the motion. Sandi Thompson called the roll.

Roll Call: Chris Mustain-Aye, Chairman Lillard-Aye, Commissioner Bryson-Aye, Mayor Bradshaw-Aye, Mayor Brown-Aye.

The motion passed unanimously.

Chairman Lillard adjourned the meeting at 4:07 p.m.

Approved:

David H. Lillard, Jr.
TLDA Audit Committee Chairman

Agenda Item 3a

Tennessee Comptroller of the Treasury

Financial and Compliance Audit Report

Tennessee Local Development Authority

For the Year Ended June 30, 2024

Jason E. Mumpower
Comptroller of the Treasury

Division of State Audit

Katherine J. Stickel, CPA, CGFM, *Director*

<u>**State Agency Audits**</u>
Robyn R. Probus, CPA, CFE, CGFM
Assistant Director

Tabitha Furlong, CPA, CFE
Audit Manager

Cleve Austin Birdwell, CPA
In-Charge Auditor

Erica Marche, CFE
Senior Auditor

Madison Jessee
Staff Auditor

David Cook, CPA
Technical Manager

<u>**Audit Special Teams**</u>
Amber L. Crawford, CGFM, SPHR
Assistant Director

Amanda S. Adams
Amy W. Brack
Editors

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comptroller.tn.gov/office-functions/state-audit.html

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Tennessee Comptroller of the Treasury

TENNESSEE
COMPTROLLER
OF THE TREASURY

JASON E. MUMPOWER
Comptroller

December 11, 2024

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, 2024. 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,

Katherine J. Stickel

Katherine J. Stickel, CPA, CGFM, Director
Division of State Audit

25/007b

Audit Report
Tennessee Local Development Authority
For the Year Ended June 30, 2024

Contents

TENNESSEE LOCAL DEVELOPMENT AUTHORITY

AUDIT HIGHLIGHTS

Opinions on the Financial Statements

The opinions on the financial statements are unmodified.

Audit Findings

The audit report contains no findings.

Prior Audit Findings

There were no findings in the prior audit report.

TENNESSEE
COMPTROLLER
OF THE TREASURY

JASON E. MUMPOWER
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 Audit of the Financial Statements

Opinions

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, 2024, and June 30, 2023, and the related notes to the financial statements, which collectively comprise the Tennessee Local Development Authority's basic financial statements as listed in the table of contents.

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, 2024, and June 30, 2023, 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.

Basis for Opinions

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Tennessee Local Development Authority and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions. 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 Tennessee Local Development Authority.

CORDELL HULL BUILDING | 425 Rep. John Lewis Way N. | Nashville, Tennessee 37243

Responsibilities of Management 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Tennessee Local Development Authority's ability to continue as a going concern for 12 months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions.

Reasonable assurance is a high level of assurance but is not absolute assurance and, therefore, is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- exercise professional judgment and maintain professional skepticism throughout the audit;
- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks; such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements;
- obtain an understanding of internal control relevant to the audit 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 Tennessee Local Development Authority's internal control; accordingly, no such opinion is expressed;
- evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements; and

- conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Tennessee Local Development Authority's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

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 6 through 11 be presented to supplement the basic financial statements. Such information is the responsibility of management, and, 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 audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Tennessee Local Development Authority's basic financial statements. The accompanying financial information on pages 21 through 23 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 November 27, 2024, 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, 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 Tennessee Local Development Authority's internal control over financial reporting and compliance.

Katherine J. Stickel

Katherine J. Stickel, CPA, CGFM, Director
Division of State Audit
November 27, 2024

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Management's Discussion and Analysis

As management of the Tennessee Local Development Authority (the 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, 2024, and June 30, 2023, with comparative data for the year ended June 30, 2022. 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 Programs and 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 in the past include

1) the State Loan Programs providing 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 providing 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.

	State Loan Programs			State Infrastructure Program		
	2024	2023	2022	2024	2023	2022
Number of borrowers with outstanding loans	3	3	3	1	1	1
Total number of outstanding loans	3	3	3	1	1	1
Total amount of outstanding loans (in thousands)	$324	$546	$ 778	$1,174	$1,241	$1,306
Number of outstanding loans approved in fiscal year	0	0	0	0	0	0
Amount of loans approved in fiscal year (in thousands)	$ -	$ -	$ -	$ -	$ -	$ -

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 Programs. To date, the State Loan Programs have only been utilized to make loans for the construction of water and sewer projects. A financial analysis is conducted of each loan applicant to be funded through the State Loan Programs 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 a set-aside amount 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 Programs.

During its construction phase, a project in the State Loan Programs is typically funded with the proceeds from the issuance of Bond Anticipation Notes. As projects reach completion, and the amount of dollars expended is evaluated 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 Programs facilities long-term fixed-rate debt range from a low of 4.2% to a high of 4.375%. By pooling the financing of the capital projects, 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, 2024, the Authority's State Loan Programs were rated AA by S&P Global (S&P) and AA by Fitch Ratings. 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 existed 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 generate 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 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 when cash is received or paid. Using the economic resources measurement focus, a reader is presented with 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 are comprised 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 borrowers with timely access to the capital markets at the lowest possible cost and to make creditworthy loans. There have been no incidents that 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 to pay debt service.

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

Statement of Net Position Summary
(Expressed in Thousands)

	2024	2023	2022
Current assets	$ 20,110	$ 18,473	$ 17,164
Restricted assets	269	273	273
Other assets	1,250	1,479	1,787
Total assets	21,629	20,225	19,224
Current liabilities	407	386	366
Noncurrent liabilities	311	555	794
Total liabilities	718	941	1,160
Net position (unrestricted)	$ 20,911	$ 19,284	$ 18,064

Note: The Authority owns no capital assets.

For the years ended June 30, 2024; June 30, 2023; and June 30, 2022, the largest component of the total asset balance is the cash balance. Loans receivable (both current and noncurrent) totaled $1,498,371 at June 30, 2024; $1,786,814 at June 30, 2023; and $2,083,768 at June 30, 2022. While loans receivable will continue to decline unless new loans are made, administrative fees collected from the State Revolving Fund (SRF) loan program have contributed to an increase in assets along with higher interest income from increasing market interest rates. Restricted assets represent the debt service reserve fund. The Authority's liabilities consist mostly of the outstanding portion of its bonds payable, which will continue to decline as debt service payments are made. Readers can refer to Note 5 in the notes to the financial statements for information on debt 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 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 meet their needs at this time.

Statements of Revenues, Expenses, and Changes in Net Position Summary
(Expressed in Thousands)

	2024	2023	2022
Operating Revenues			
Revenue from loans	$ 56	$ 69	$ 82
Administrative fees collected	784	729	651
Interest income	1,017	654	35
Total operating revenues	1,857	1,452	768
Operating Expenses			
Interest expense	31	41	49
Subsidy to borrowers	19	13	1
Administrative expenses	180	178	153
Total operating expenses	230	232	203
Operating income	1,627	1,220	565
Increase in Net Position	$ 1,627	$ 1,220	$ 565

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 of and authority to approve loans made from the Clean Water and Drinking Water 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 from loans decreased from 2023 to 2024 and decreased from 2022 to 2023. Interest income increased during the periods shown as market interest rates increased. Administrative fees related to the SRF loan programs also increased during the periods shown. Revenue from loans of the Authority is declining as the State Loan Programs wind down. All the Authority's loans are structured such that the borrowers make level debt service payments for the life of the loan, meaning that over time as the borrowers' principal portion of the payment increases, the interest portion of the payment decreases. Because no new loans have been made, as the existing loans approach maturity, the interest revenue will trend downward. The Authority's total operating expenses slightly decreased from 2023 to 2024 and increased from 2022 to 2023. The increase in operating expenses from 2022 to 2023 is attributed to a high-interest rate environment that increased the amount of subsidies due to borrowers and to increased costs of administering the State Revolving Fund loan programs. Market interest rates remained high in fiscal year 2024. Unless new loans are made, interest expense related to the State Loan Programs is expected 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 Division of State Government Finance, State of Tennessee, Cordell Hull Building, 425 Rep. John Lewis Way N., Nashville, Tennessee 37243-3400 or visit our website at http://www.comptroller.tn.gov/sl/.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Statements of Net Position
June 30, 2024, and June 30, 2023

(Expressed in Thousands)

	June 30, 2024	June 30, 2023
Assets		
Current assets:		
Cash and cash equivalents (Notes 1 and 2)	$ 19,862	$ 18,165
Receivables:		
Loans receivable	248	308
Total current assets	20,110	18,473
Noncurrent assets:		
Restricted cash (Notes 2 and 3)	269	273
Loans receivable	1,250	1,479
Total noncurrent assets	1,519	1,752
Total assets	21,629	20,225
Liabilities		
Current liabilities:		
Accrued interest payable	8	11
Payable to borrowers (Note 4)	154	135
Revenue bonds payable (Note 5)	245	240
Total current liabilities	407	386
Noncurrent liabilities:		
Revenue bonds payable, net (Note 5)	311	555
Total noncurrent liabilities	311	555
Total liabilities	718	941
Net position		
Unrestricted (Note 6)	20,911	19,284
Total net position	$ 20,911	$ 19,284

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, 2024, and June 30, 2023

(Expressed in Thousands)

	Year Ended June 30, 2024	Year Ended June 30, 2023
Operating revenues		
Revenue from loans	$ 56	$ 69
Administrative fees collected	784	729
Interest income	1,017	654
Total operating revenues	1,857	1,452
Operating expenses		
Interest expense	31	41
Subsidy to borrowers	19	13
Administrative expenses	180	178
Total operating expenses	230	232
Operating income	1,627	1,220
Net position		
Net position, July 1	19,284	18,064
Net position, June 30	$ 20,911	$ 19,284

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, 2024, and June 30, 2023

(Expressed in Thousands)

	Year Ended June 30, 2024	Year Ended June 30, 2023
Cash flows from operating activities		
Payments to service providers	$ (180)	$ (178)
Net cash used for operating activities	(180)	(178)
Cash flows from noncapital financing activities		
Principal payments	(240)	(230)
Interest paid	(33)	(43)
Net cash used for noncapital financing activities	(273)	(273)
Cash flows from investing activities		
Collections of loan principal	289	297
Interest received on loans	56	69
Administrative revenue	784	729
Interest received on pooled investment fund	1,017	654
Net cash provided by investing activities	2,146	1,749
Net increase in cash	1,693	1,298
Cash and cash equivalents, July 1	18,438	17,140
Cash and cash equivalents, June 30	$ 20,131	$ 18,438
Reconciliation of operating income to net cash used for operating activities:		
Operating income	$ 1,627	$ 1,220
Adjustments to reconcile operating income to net cash used for operating activities:		
Revenue from loans	(56)	(69)
Administrative revenue from borrowers	(784)	(729)
Interest income	(1,017)	(654)
Interest expense	31	41
Subsidy to borrowers	19	13
Total adjustments	(1,807)	(1,398)
Net cash used for operating activities	$ (180)	$ (178)

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

Note 1. Summary of Significant Accounting Policies

Reporting Entity

The Tennessee Local Development Authority (The 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, intellectual and developmental disability, 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 No. 14, *The Financial Reporting Entity*, as amended, the Authority is discretely presented in Tennessee's *Annual Comprehensive 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 Division of State Government Finance serves as the assistant secretary, and the finance staff within the Division of State Government 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 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 description are reported as nonoperating revenues and expenses.

Cash and Cash Equivalents

This classification includes deposits in demand accounts, as well as short-term investments with a maturity date within three months of the date acquired by the state.

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 and Investments

Under the Authority's General Bond Resolution, the Authority's funds are to be held and invested by the State Treasurer.

The Authority's cash is invested in the State Pooled Investment Fund (SPIF) administered by the State Treasurer. The Authority had $20,131,230 in the SPIF at June 30, 2024, and $18,438,480 at June 30, 2023. 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. The pooled investment fund's investment policy and required risk disclosures are presented in the SPIF financial statements and notes, which are available on the state's website at https://treasury.tn.gov/Explore-Your-TN-Treasury/About-the-Treasury/Department-Reports.

Note 3. Restricted Assets

The Authority's General Bond Resolution 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 $268,703 at June 30, 2024, and $273,603 at June 30, 2023.

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.

Note 5. Debt Payable

Revenue Bonds

Bonds payable at June 30, 2024, and June 30, 2023, were as follows (expressed in thousands):

	June 30, 2024	June 30, 2023
2006 Series B at interest rates from 4.2% to 4.375% maturing to 2029 (original par-$37,415)	$560	$ 800
Total par amount of bonds payable	560	800
Less unamortized discount	(4)	(5)
Net bonds payable	$556	$ 795

Debt service requirements to maturity of the revenue bonds payable at June 30, 2024, were as follows (expressed in thousands):

For the Year(s) Ending June 30	Principal	Interest	Total
2025	245	24	269
2026	260	13	273
2027	15	2	17
2028	20	2	22
2029	20	1	21
Total	$ 560	$ 42	$ 602

Changes in long-term debt payable for the year ended June 30, 2024, were as follows (expressed in thousands):

	Balance July 1, 2023	Additions	Reductions	Balance June 30, 2024	Amounts Due Within One Year
Revenue bonds payable	$ 800	$ -	$ 240	$ 560	$ 245
Less: unamortized bond discount	(5)	-	(1)	(4)	-
Total bonds payable	$ 795	$ -	$ 239	$ 556	$ 245

Changes in long-term debt payable for the year ended June 30, 2023, are as follows (expressed in thousands):

	Balance July 1, 2022	Additions	Reductions	Balance June 30, 2023	Amounts Due Within One Year
Revenue bonds payable	$ 1,030	$ -	$ 230	$ 800	$ 240
Less: unamortized bond discount	(6)	-	(1)	(5)	-
Total bonds payable	$ 1,024	$ -	$ 229	$ 795	$ 240

Events of Default

Debt outstanding under the Tennessee Local Development Authority State Loan Programs 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.

In the 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 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 by 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 has 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, 2024, the statutory reserve balance was $3,625,537.

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 its loan timely. 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 by the statutory reserve.

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 financial 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 2024 and 2023, no loans were made or approved.

TENNESSEE LOCAL DEVELOPMENT AUTHORITY

Supplementary Schedules of Net Position - Program Level

June 30, 2024, and June 30, 2023

(Expressed in Thousands)

	June 30, 2024			June 30, 2023		
	State Loan Programs	State Infrastructure Loan Program	Total	State Loan Programs	State Infrastructure Loan Program	Total
Assets						
Current assets:						
Cash and cash equivalents	$ 18,458	$ 1,404	$ 19,862	$ 16,921	$ 1,244	$ 18,165
Receivables:						
Loans receivable	180	68	248	241	67	308
Total current assets	18,638	1,472	20,110	17,162	1,311	18,473
Noncurrent assets:						
Restricted cash	269	-	269	273	-	273
Loans receivable	144	1,106	1,250	305	1,174	1,479
Total noncurrent assets	413	1,106	1,519	578	1,174	1,752
Total assets	19,051	2,578	21,629	17,740	2,485	20,225
Liabilities						
Current liabilities:						
Accrued interest payable	8	-	8	11	-	11
Payable to borrowers	154	-	154	135	-	135
Revenue bonds payable	245	-	245	240	-	240
Total current liabilities	407	-	407	386	-	386
Noncurrent liabilities:						
Revenue bonds payable, net	311	-	311	555	-	555
Total noncurrent liabilities	311	-	311	555	-	555
Total liabilities	718	-	718	941	-	941
Net position						
Unrestricted	18,333	2,578	20,911	16,799	2,485	19,284
Total net position	$ 18,333	$ 2,578	$ 20,911	$ 16,799	$ 2,485	$ 19,284

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Supplementary Schedules of Revenues, Expenses, and Changes in Net Position - Program Level
For the Years Ended June 30, 2024, and June 30, 2023

(Expressed in Thousands)

	Year Ended June 30, 2024			Year Ended June 30, 2023		
	State Loan Programs	State Infrastructure Loan Program	Total	State Loan Programs	State Infrastructure Loan Program	Total
Operating revenues						
Revenue from loans	$ 33	$ 23	$ 56	$ 45	$ 24	$ 69
Administrative fees collected	783	1	784	727	2	729
Interest income	948	69	1,017	611	43	654
Total operating revenues	1,764	93	1,857	1,383	69	1,452
Operating expenses						
Interest expense	31	-	31	41	-	41
Subsidy to borrowers	19	-	19	13	-	13
Administrative expenses	180	-	180	178	-	178
Total operating expenses	230	-	230	232	-	232
Operating income	1,534	93	1,627	1,151	69	1,220
Net position						
Net position, July 1	16,799	2,485	19,284	15,648	2,416	18,064
Net position, June 30	$ 18,333	$ 2,578	$ 20,911	$ 16,799	$ 2,485	$ 19,284

TENNESSEE LOCAL DEVELOPMENT AUTHORITY
Supplementary Schedules of Cash Flows - Program Level
For the Years Ended June 30, 2024, and June 30, 2023

(Expressed in Thousands)

	Year Ended June 30, 2024			Year Ended June 30, 2023		
	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	$ (180)	$ -	$ (180)	$ (178)	$ -	$ (178)
Net cash used for operating activities	(180)	-	(180)	(178)	-	(178)
Cash flows from noncapital financing activities						
Principal payments	(240)	-	(240)	(230)	-	(230)
Interest paid	(33)	-	(33)	(43)	-	(43)
Net cash used for noncapital financing activities	(273)	-	(273)	(273)	-	(273)
Cash flows from investing activities						
Collections of loan principal	222	67	289	232	65	297
Interest received on loans	33	23	56	45	24	69
Administrative revenue	783	1	784	727	2	729
Interest received on pooled investment fund	948	69	1,017	611	43	654
Net cash provided by investing activities	1,986	160	2,146	1,615	134	1,749
Net increase in cash	1,533	160	1,693	1,164	134	1,298
Cash, July 1	17,194	1,244	18,438	16,030	1,110	17,140
Cash, June 30	$ 18,727	$ 1,404	$ 20,131	$ 17,194	$ 1,244	$ 18,438
Reconciliation of operating income to net cash used for operating activities:						
Operating income	$ 1,534	$ 93	$ 1,627	$ 1,151	$ 69	$ 1,220
Adjustments to reconcile operating income to net cash used for operating activities:						
Revenue from loans	(33)	(23)	(56)	(45)	(24)	(69)
Administrative revenue from borrowers	(783)	(1)	(784)	(727)	(2)	(729)
Interest income	(948)	(69)	(1,017)	(611)	(43)	(654)
Interest expense	31	-	31	41	-	41
Subsidy to borrowers	19	-	19	13	-	13
Total adjustments	(1,714)	(93)	(1,807)	(1,329)	(69)	(1,398)
Net cash used for operating activities	$ (180)	$ -	$ (180)	$ (178)	$ -	$ (178)

JASON E. MUMPOWER
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, 2024, and the related notes to the financial statements, which collectively comprise the Tennessee Local Development Authority's basic financial statements, and have issued our report thereon dated November 27, 2024. 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.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Tennessee Local Development 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 Tennessee Local Development Authority's internal control. Accordingly, we do not express an opinion on the effectiveness of the Tennessee Local Development 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.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Tennessee Local Development Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts (including 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.

Katherine J. Stickel

Katherine J. Stickel, CPA, CGFM, Director
Division of State Audit
November 27, 2024

Agenda Item 3b

Tennessee Comptroller of the Treasury

Financial and Compliance Audit Report

Clean Water State Revolving Fund

For the Year Ended June 30, 2024

Jason E. Mumpower
Comptroller of the Treasury

Division of State Audit

Katherine J. Stickel, CPA, CGFM, *Director*

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JASON E. MUMPOWER
Comptroller

December 11, 2024

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, 2024. 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,

Katherine J. Stickel, CPA, CGFM, Director
Division of State Audit

25/007a

Audit Report

Clean Water State Revolving Fund

For the Year Ended June 30, 2024

Contents

CLEAN WATER STATE REVOLVING FUND

AUDIT HIGHLIGHTS

Opinions on the Financial Statements

The opinions on the financial statements are unmodified.

Audit Findings

The audit report contains no findings.

Prior Audit Findings

There were no findings in the prior audit report.

TENNESSEE
COMPTROLLER
OF THE TREASURY

JASON E. MUMPOWER
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 Audit of the Financial Statements

Opinions

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, 2024, and June 30, 2023, and the related notes to the financial statements, which collectively comprise the fund's basic financial statements as listed in the table of contents.

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 as of June 30, 2024, and June 30, 2023, 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.

Basis for Opinions

We conducted our audit in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Clean Water State Revolving Fund and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions. 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.

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Responsibilities of Management 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Clean Water State Revolving Fund's ability to continue as a going concern for 12 months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinions.

Reasonable assurance is a high level of assurance but is not absolute assurance and, therefore, is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we

- exercise professional judgment and maintain professional skepticism throughout the audit;
- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks; such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements;
- obtain an understanding of internal control relevant to the audit 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 Clean Water State Revolving Fund's internal control; accordingly, no such opinion is expressed;
- evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements; and

- conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Clean Water State Revolving Fund's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Emphasis of Matters

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, 2024, and June 30, 2023, 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, 2024, 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 Clean Water State Revolving Fund's internal control over financial reporting and compliance.

Katherine J. Stickel, CPA, CGFM, Director
Division of State Audit
November 27, 2024

CLEAN WATER STATE REVOLVING FUND
Statements of Net Position
June 30, 2024, and June 30, 2023

(Expressed in Thousands)

	June 30, 2024	June 30, 2023
Assets		
Current assets:		
Cash and cash equivalents (Notes 1 and 2)	$ 412,164	$ 366,555
Loans receivable	52,139	47,248
Total current assets	464,303	413,803
Noncurrent assets:		
Loans receivable	841,596	829,695
Total noncurrent assets	841,596	829,695
Total assets	1,305,899	1,243,498
Liabilities		
Current liabilities:		
Payable to borrowers (Note 3)	309	156
Due to general fund	40	23
Total current liabilities	349	179
Noncurrent liabilities:		
Customer deposits payable (Note 2)	6,502	4,229
Total noncurrent liabilities	6,502	4,229
Total liabilities	6,851	4,408
Net position		
Unrestricted	1,299,048	1,239,090
Total net position	$ 1,299,048	$ 1,239,090

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, 2024, and June 30, 2023

(Expressed in Thousands)

	Year Ended June 30, 2024	Year Ended June 30, 2023
Operating revenues		
Revenue from loans	$ 10,748	$ 10,505
Interest income	19,509	13,061
Total operating revenues	30,257	23,566
Operating expenses		
Administrative expenses	904	1,082
Total operating expenses	904	1,082
Operating income	29,353	22,484
Nonoperating revenues		
Capitalization grant	24,368	957
Total nonoperating revenues	24,368	957
Nonoperating expenses		
Principal forgiveness (Note 5)	2,123	293
Total nonoperating expenses	2,123	293
Income before transfers	51,598	23,148
Transfers in (Note 4)	8,360	6,892
Change in net position	59,958	30,040
Net position, July 1	1,239,090	1,209,050
Net position, June 30	$ 1,299,048	$ 1,239,090

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, 2024, and June 30, 2023

(Expressed in Thousands)

	Year Ended June 30, 2024	Year Ended June 30, 2023
Cash flows from operating activities		
Payments for interfund services	$ (887)	$ (1,093)
Net cash used for operating activities	(887)	(1,093)
Cash flows from noncapital financing activities		
Operating grants received	24,368	957
Transfers in	8,360	6,892
Net cash provided by noncapital financing activities	32,728	7,849
Cash flows from investing activities		
Loans issued and other disbursements to borrowers	(69,348)	(78,516)
Collections of loan principal	50,114	43,566
Security deposits from borrowers	2,712	324
Interest received on loans	10,748	10,505
Interest received on investments	19,818	13,217
Amounts repaid to borrowers	(276)	(18)
Net cash provided by (used for) investing activities	13,768	(10,922)
Net increase (decrease) in cash	45,609	(4,166)
Cash and cash equivalents, July 1	366,555	370,721
Cash and cash equivalents, June 30	$ 412,164	$ 366,555
Reconciliation of operating income to net cash used for operating activities:		
Operating income	$ 29,353	$ 22,484
Adjustments to reconcile operating income to net cash used for operating activities:		
Revenue from loans	(10,748)	(10,505)
Interest income	(19,509)	(13,061)
Increase (decrease) due to general fund	17	(11)
Total adjustments	(30,240)	(23,577)
Net cash used for operating activities	$ (887)	$ (1,093)
Noncash investing transactions		
Application of security deposits to loans	$ 319	$ -

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, 2024, and June 30, 2023

Note 1. Summary of Significant Accounting Policies

Reporting Entity

The Clean Water State Revolving Fund (CWSRF) was created to provide local governments and utility districts with low-cost financial assistance to improve and protect water quality and public health. The CWSRF has been included in Tennessee's *Annual Comprehensive Financial Report* as an enterprise fund (the Sewer Treatment Loan Fund). That report is posted on the state's website at https://www.tn.gov/finance/rd-doa/fa-accfin-ar.html.

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 when liabilities are incurred, regardless of the timing of related cash flows.

Operating revenues and expenses are distinguished from nonoperating items in the CWSRF. 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 and Cash Equivalents

This classification includes deposits in demand accounts as well as short-term investments with a maturity date within three months of the date acquired by the state.

Note 2. Deposits and Investments

The Authority's cash is invested in the State Pooled Investment Fund (SPIF) administered by the State Treasurer. Cash used for operating purposes is invested in the SPIF, and customer security deposits are invested in the Local Government Investment Pool (LGIP), which is part of the SPIF. The CWSRF had $405,661,585 in the SPIF for operating cash purposes and $6,502,422 in customer security deposits in the LGIP at June 30, 2024, and the fund had $362,325,530 in the SPIF and $4,229,170 in the LGIP at June 30, 2023. 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. The pooled investment fund's investment policy and required risk disclosures are presented in the SPIF financial statements and notes, which are available on the state's website at https://treasury.tn.gov/Explore-Your-TN-Treasury/About-the-Treasury/Department-Reports.

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 CWSRF 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 CWSRF received an interfund transfer of $8,360,700 from the state's general fund during the year ended June 30, 2024, and $6,891,600 during the year ended June 30, 2023.

Note 5. Principal Forgiveness

In fiscal year 2010, the CWSRF received money from the American Recovery and Reinvestment Act (ARRA) of 2009. As part of the conditions stipulated by ARRA 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 CWSRF 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 subsidy are determined according to standard procedures of priority ranking previously established by the Tennessee Department of Environment and Conservation (TDEC) when making loans. Principal forgiveness is recognized on the statements of cash flows as part of "loans issued and other disbursements to borrowers."

Note 6. Subsequent Events

On September 26-27, 2024, Hurricane Helene hit the East Tennessee region as a tropical storm. On October 2, 2024, eight Tennessee counties were listed in an Expedited Major Disaster Declaration following historic flooding. TDEC identified multiple water and wastewater systems in the declared disaster area, some of which included Tennessee's State Revolving Fund (SRF) customers. On October 2, 2024, board members of the Tennessee Local Development Authority approved emergency actions to be taken, as allowed by the EPA and recommended by TDEC, with the intent to provide relief to SRF borrowers that included 12 months of loan payment forbearance.

TENNESSEE
COMPTROLLER
OF THE TREASURY

JASON E. MUMPOWER
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, an enterprise fund of the State of Tennessee, as of and for the year ended June 30, 2024, and the related notes to the financial statements, which collectively comprise the Clean Water State Revolving Fund's basic financial statements, and have issued our report thereon dated November 27, 2024. 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.

Report on 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 Clean Water State Revolving Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Clean Water State Revolving 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.

Report on 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.

Kathy J. Stickel

Katherine J. Stickel, CPA, CGFM, Director
Division of State Audit
November 27, 2024

Agenda Item 4

Jason E. Mumpower
Comptroller

Fiscal Year Ending June 30, 2024

TLDA Programs

1. State Loan Program Fund (Water/Sewer)
   - 3 borrowers
   - 3 loans outstanding
   - $560,000 bonds outstanding (Bonds mature 2029)

2. State Infrastructure Fund (Transportation)
   - 1 borrower
   - Amounts Collected
     - $66,667 loan principal
     - $22,884 interest

Operating Income: $1,627,624
Net Position at June 30, 2024: $20,912,060

No new loans are currently being issued for these programs. However, the state's FY 2026 budget includes a $50 million non-recurring appropriation for the State Infrastructure Fund.

State Revolving Fund Loan Programs

1. Clean Water Fund
   - Disbursements
     - $69,030,193
   - Amounts Collected
     - $49,795,760 loan principal
     - $10,747,998 interest
   - Net position at June 30, 2024: $1,299,047,731

2. Drinking Water Fund
   - Disbursements
     - $50,643,889
   - Amounts Collected
     - $8,033,335 loan principal
     - $1,528,956 interest
   - Net position at June 30, 2024: $279,035,432

No significant changes to accounting and reporting standards.

Agenda Item 5a

Department of Environment & Conservation

TLDA Audit Committee Meeting
June 23, 2025

Clean Water State Revolving Fund Loan Program
EPA Program Evaluation Summary SFY 2023

On May 28, 2024, EPA conducted an Annual Review Opening Meeting for the Clean Water SRF. This is a Program Evaluation. On September 23, 2024, the review concluded with a Closing Meeting. EPA identified no findings or required actions. EPA did make several recommendations. Those recommendations are included in this summary report as well as the TDEC SRF response.

EPA Recommendation: EPA recommends that the Tennessee Department of Environment and Conservation evaluate ways to reduce the cash-to-average annual disbursement ratio below two years. At this time, the preeminent recommendation for doing so includes evaluating projects for readiness to proceed to construction.

TDEC SRF Response: In late winter of 2024, SRF established new Readiness To Proceed criteria detailed in our Intended Use Plan (IUPs) and demonstrated in our Priority Ranking List (PRLs) with an "above the ranking line" vs "below the ranking line" breakpoint. Entities above the ranking line have demonstrated a readiness to proceed and are invited to complete the SRF loan process. This helps ensure projects that proceed through the loan process are ready to proceed. For additional information on Readiness To Proceed, please refer to the SRF Intended Use Plans.

EPA Recommendation: EPA recommends TDEC SRF implement higher salary grades and/or increase salaries to hire specialized SRF staff to help the state maintain a fully staffed programmatic and engineering team to maintain best practices and mitigate risks to the program.

TDEC SRF Response: We are nearly fully staffed. SRF is practicing hiring at 85% above base for selected applicants. We continue to search for and hire applicants with experience and aim for a salary start near midpoint.

EPA Recommendations: TDEC SRF should document its plan to move money into loans through IUPs.

TDEC SRF Response: In late SFY 2024 TDEC SRF released the Questionnaire through a *Grants Management System.* This online system improves the customer experience and provides an efficient way to communicate process steps and keep customers informed. The program also developed a phased approach to moving applicants through the loan process. Further, SRF is undergoing a Business Process Improvement plan, overhauling the fundamentals of the program, eliminating unnecessary requirements and aligning with federal minimum requirements. These steps will take at least two years to have a noticeable impact on improving the movement of funding through loan agreements. We should start to see significant improvements in SFY 2027.

EPA Recommendations: TDEC SRF should ensure that all relevant data for assistance agreements are consistently entered in the OWSRF database, including the associated fiscal year appropriation grant and the assigned additional subsidization.

TDEC SRF Response: SRF and SWIG are actively working to train all staff on how to use the new EPA database system, OWSRF, and when/how data should be entered. We are also rectifying older entries. We have established a monthly OWSRF data entry task for all teams.

EPA Recommendation: TDEC SRF consider having the assistance applicant's engineer provide a certification on the useful life of the infrastructure that will be financed with the SRF loan. This will provide a check on the requirement that the loan term does not exceed the useful life of the infrastructure.

TDEC SRF Response: We will consider incorporating this recommendation into our process during the business process improvement work.

EPA Recommendation: TDEC SRF should utilize a Green Project Reserve (GPR) Determination checklist when processing applications to assist with ensuring the correct loan amounts and GPR category are being assigned and entered into the OWSRF database.

TDEC SRF Response: We will consider incorporating this recommendation into our process during the business process improvement work.

EPA Recommendation: EPA recommends that TDEC SRF includes BABA waiver documentation in all project files for projects eligible for the design planning waiver.

TDEC SRF Response: BABA is a newer federal requirement and training for states on implementation has been confusing and inconsistent. We have requested EPA provide TDEC SRF staff BABA specific training to ensure our customers and our SRF loan files are meeting minimum federal requirements.

EPA Recommendation: EPA recommends that TDEC SRF require assistance recipients to comply with the prohibition on certain telecommunication and video surveillance services or equipment in accordance with 2 CFR 200.216, which implements section 889 of Public Law 115-232, into loan agreements for equivalency projects.

TDEC SRF Response: SRF's loan agreements are currently under review by TDEC's Office of General Counsel (OGC). OGC is ensuring contracts meet the minimum federal requirements, including compliance with recent Executive Orders.

EPA Recommendation: EPA recommends that TDEC SRF state the assistant recipient's revenue repayment source in the financial analysis approval letter.

TDEC SRF Response: We will consider incorporating this recommendation into our process during the business process improvement work.

EPA Recommendation: EPA recommends that TDEC SRF update their standard signage templates for both non-BIL base equivalency projects to meet EPA's Guidelines for Enhancing Public Awareness of SRF Assistance Agreements (2015) and BIL-funded projects to meet EPA's Guidelines for Implementing the BIL Signage Term and Condition for SRF Programs (2022).

TDEC SRF Response: TDEC SRF has made this update.

EPA Recommendation: EPA recommends that TDEC SRF update their Standard Operating Procedures, internal guidance documents, and/or inspection checklists to list the five requirements of American Iron and Steel certification letters to help better ensure all letters are accurate and complete.

TDEC SRF Response: We will incorporate these recommendations into our process during the business process improvement work.

EPA Recommendation: TDEC SRF should continue working to ensure compliance with the requirements of the Federal Flood Risk Management Standard, including documenting the approved floodplain determination method used and public notice procedures in the environmental determination.

TDEC SRF Response: We continue to ensure compliance with these requirements.

EPA Recommendation: EPA recommends that TDEC SRF demonstrate which agencies are being consulted with for each of the environmental crosscutting authorities to ensure that each of the required environmental crosscutters are being reviewed.

TDEC SRF Response: We will incorporate these recommendations into our process during the business process improvement work.

CWSRF Follow-up on SFY 2022 Recommendations

- EPA recommended CWSRF work to reduce the balance of uncommitted funds, which at the time of the review was approximately $161 million dollars. TDEC SRF has increased the number of loans awarded by increasing demand through education, outreach, technical assistance, and other actions; however, TDEC SRF's uncommitted funds balance in SFY23 has increased to $210 million dollars. TDEC SRF continues to increase community engagement, improve loan program processes, and develop a strategy for small and disadvantaged communities.
- EPA recommended CWSRF work to maintain a fully staffed program and engineering team to mitigate any risk to the program. TDEC SRF has hired seven new staff since the SFY22 CWSRF PER

and currently has multiple open positions being recruited and interviewed. TDEC SRF is also pursuing a contract with an outside firm to assist with site inspections and other project management related duties until all positions are filled.

- EPA recommended CWSRF implement an SOP to streamline American Iron and Steel letter review and requirements to ensure borrowers follow EPA guidelines. TDEC SRF has retrained technical staff on the requirements for AIS requirements, but EPA Region 4 personnel noted during project file reviews that some AIS letters missed some of the required elements.

Drinking Water State Revolving Fund Loan Program
EPA Program Evaluation Summary SFY 2023

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TDEC SRF Response: We will consider incorporating this recommendation into our process during the business process improvement work.

EPA Recommendation: TDEC SRF should utilize a Green Project Reserve (GPR) Determination checklist when processing applications to assist with ensuring the correct loan amounts and GPR category are being assigned and entered into the OWSRF database.

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EPA Recommendation: EPA recommends that TDEC SRF update their standard signage templates for both non-BIL base equivalency projects to meet EPA's Guidelines for Enhancing Public Awareness of SRF

Assistance Agreements (2015) and BIL-funded projects to meet EPA's Guidelines for Implementing the BIL Signage Term and Condition for SRF Programs (2022).

TDEC SRF Response: TDEC SRF has made this update.

EPA Recommendation: EPA recommends that TDEC SRF update their Standard Operating Procedures, internal guidance documents, and/or inspection checklists to list the five requirements of American Iron and Steel certification letters to help better ensure all letters are accurate and complete.

TDEC SRF Response: We will incorporate these recommendations into our process during the business process improvement work.

EPA Recommendation: EPA recommends that TDEC SRF update their SOPs and/or internal guidance documents to ensure that Technical, Managerial, and Financial Capacity is completed for all DWSRF projects before receiving financial assistance, including funds for studies, planning, and design.

TDEC SRF Response: We will incorporate these recommendations into our process during the business process improvement work.

EPA Recommendation: TDEC SRF should continue working to ensure compliance with the requirements of the Federal Flood Risk Management Standard, including documenting the approved floodplain determination method used and public notice procedures in the environmental determination.

TDEC SRF Response: We continue to ensure compliance with these requirements.

EPA Recommendation: EPA recommends that TDEC SRF demonstrate which agencies are being consulted with for each of the environmental crosscutting authorities to ensure that each of the required environmental crosscutters are being reviewed.

TDEC SRF Response: We will incorporate these recommendations into our process during the business process improvement work.

Drinking Water SRF Follow-up on SFY 2022 Recommendations

- EPA recommended TDEC SRF work to increase the pace of loan execution and fund distribution. TDEC SRF has increased the number of loans awarded by increasing demand through education, outreach, technical assistance, and other actions. TDEC SRF is also undergoing a program overhaul with significant business process improvements scheduled for the next two years. TDEC SRF continues to increase community engagement, improve loan program processes, and develop a strategy for small and disadvantaged communities.

- EPA recommended DWSRF work to maintain a fully staffed program and engineering team to mitigate any risk to the program. TDEC SRF has hired seven new staff since the SFY22 CWSRF PER and currently has multiple open positions being recruited and interviewed. TDEC SRF is also pursuing a contract with an outside firm to assist with site inspections and other project management related duties until all positions are filled.
- EPA recommended CWSRF implement an SOP to streamline American Iron and Steel letter review and requirements to ensure borrowers follow EPA guidelines. TDEC SRF has retrained technical staff on the requirements for AIS requirements, but EPA Region 4 personnel noted during project file reviews that some AIS letters missed some of the required elements.

Agenda Item 5b

U. S. ENVIRONMENTAL PROTECTION AGENCY
REGION 4
PROGRAM EVALUATION REPORT
OCTOBER 8, 2024

Tennessee Drinking Water State Revolving Fund
State Fiscal Year 2023
July 1, 2022 – June 30, 2023

Contents

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 TDEC's fiscal year (FY) 2023, which runs from July 1, 2022, to June 30, 2023. The U.S. Environmental Protection Agency (EPA) is required by 40 CFR § 35.3570 to annually assess the success of TDEC's performance of activities to determine compliance with the terms of the capitalization grant agreement. In part, the EPA utilized TDEC's FY22 DWSRF Intended Use Plans (IUPs) and FY23 annual reports in its review.

On November 15, 2021, the President signed P.L. 117-58, the "Bipartisan Infrastructure Law (BIL), also known as the "Infrastructure Investment and Jobs Act of 2021" (IIJA) into law. EPA awarded BIL supplemental capitalization grants through the state's DWSRF program for water infrastructure projects.

The EPA Federal FY22 Base capitalization grant provided Tennessee with $12,172,000 in drinking water assistance. This required a 20 percent state match of $2,424,400. When added to the DWSRF capitalization grant the total available for assistance is $14,606,400.

The EPA Federal FY22 BIL General Supplemental (GS) capitalization grant provided Tennessee with $31,253,000 in drinking water assistance. This required a 10 percent state match, $3,125,300. When added to the DWSRF capitalization grant the total available for assistance is $34,378,300.

The EPA Federal FY22 BIL Lead Service Line Replacement (LSLR) capitalization grant provided Tennessee with $49,243,000 in drinking water assistance. As there was no required state match, this amount is the total available for assistance. No LSLR assistance agreements were executed by TDEC during FY23.

The EPA Federal FY22 BIL Emerging Contaminants (EC) capitalization grant provided Tennessee with $13,123,000 in drinking water assistance. As there was no required state match, this amount is the total available for assistance. No EC assistance agreements were executed by TDEC during FY23.

During FY23, TDEC made 11 new loans to local governments totaling $46,820,111.24 One of the metrics the EPA utilizes in evaluating state programs is Pace, which is defined as cumulative amount of loans issued as a percentage of all funds available. As of June 30, 2023, the reported pace of TDEC's program was 69 percent, a decrease from TDEC's FY22 program pace of 73 percent. The national average for FY23 is 95 percent.

The Tennessee DWSRF has been administered in accordance with Section 1452 of the Safe Drinking Water Act (SDWA) as amended. The program is following all terms, schedules, provisions/assurances of the IUP, the operating agreement between TDEC and the EPA, and the conditions of the capitalization grant agreement.

SECTION I: PURPOSE AND SCOPE

The EPA Region 4 began the FY23 annual review of the Tennessee DWSRF with an opening meeting on May 28, 2024. The review concluded with a closing conference on September 23, 2024. This review process was conducted as prescribed in Section 1452 of the SDWA, 40 CFR § 35.3575 and in the Annual Review Guidance issued October 2023. The review was conducted in a hybrid approach, both virtually and in person.

The purposes of the annual review are to:

1. Evaluate the success of the state's performance in achieving goals and objectives identified in the IUP, and the state's annual report;

2. Evaluate the state's compliance with regulations, operating agreement, and capitalization grant agreement;

3. Assess the financial status and performance of the fund;

4. Review the program in accordance with EPA's SRF Annual Review Guidance;

5. Review the status of resolution of prior year PER findings; and

6. Examine and follow up on any open audit findings and recommendations.

In attendance at the opening conference for TDEC were Vena Jones, Felicia Freeman, Lacey Black, and Paula Mitchell. Attending from the EPA Region 4 were Brooke Pine, Chris Bruegge, and Jill Causse. Attending from EPA Headquarters were Kelly Tucker, Howard Rubin, and Logan Loadholtz.

During the review period, EPA Region 4 examined project files, loan agreements, any additional supporting documents, and met with TDEC staff to better understand issues and exchange information. EPA Contractors, meanwhile, tested financial transactions.

At the completion of the review, a virtual exit briefing was held to review the observations made by the EPA and to clarify any outstanding issues. Attending the exit conference for TDEC were Paula Mitchell, Vena Jones, and Lacey Black. Attending from the EPA Region 4 were Johnnie Purify, Mara Lindsley, Jill Causse, Tracy Williams, Chris Bruegge, Vincent Harvey, and Ronekisha Oliver.

SECTION II: COMPLIANCE REQUIREMENTS

TDEC provided the EPA with the most recent financial audit for the year ending June 30, 2023. This audit, dated December 2023, contained no findings.

TDEC is in compliance with the Disadvantaged Business Enterprise (DBE) requirement detailed in their capitalization grant award. TDEC's DBE participation for the most recent reporting year was 0.20 percent. TDEC provides assurances that borrowers follow the six affirmative steps for DBE participation.

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: TDEC 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: TDEC certified this in the FY22 IUPs.

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

   Status: TDEC has provided an assurance to this effect in its Operating Agreement, which states that TDEC shall maintain project level controls to ensure both technical and fiscal integrity of the SRF program. TDEC is in compliance with Title XIV of the Safe Drinking Water Act and is in compliance with this assurance.

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

   Status: TDEC certified this in the FY22 IUPs.

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

   Status: TDEC has deposited the capitalization grant appropriately.

6. Assurance that the state will provide an amount equal to 20 percent of base capitalization grant and 10 percent of BIL General Supplemental capitalization grant (state match) in the fund.

   Status: The FY22 base capitalization grant was $12,172,000. The 20 percent state match amount *of $2,424,400 was provided through state appropriations. The FY22 BIL General Supplemental capitalization grant was $31,253,000. The 10 percent state match amount of $3,125,300 was provided through state appropriation funds.*

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

   Status: TDEC did not leverage. All repayments and interest earnings are credited to the fund.

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

   Status: As noted in the FY23 state audit, TDEC 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 annually. 40 CFR § 35.3570(b) states that audits are due within one year after the end of the FY.

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: TDEC 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 cumulated pace percentage for TDEC is 69 percent, a decrease from TDEC's FY22 program pace of 73 percent. TDEC disbursed a total of $20,944,962 from the DWSRF in FY23.

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

    Status: The annual report documents that TDEC is in compliance with this assurance.

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

    Status: The FY23 annual report for TDEC's DWSRF program was due to EPA on September 30, 2023. Prior to the September 30, 2023, due date, TDEC requested an extension for their annual report ending June 30, 2023, shifting their due date to October 30,2023. When the extended due date was not met, EPA Region 4 and TDEC negotiated two different estimated submittal dates, those were January 1, 2024, and March 1, 2024, neither of which were met. The report, which was received on March 19, 2024, contained adequate and accurate information regarding program implementation.

SECTION III: PROGRAM GOALS

TDEC has a number of long-term and short-term goals in their IUPs. The EPA evaluated one long-term and one short-term goal. TDEC is working toward meeting each of the goals evaluated. TDEC's status in meeting these goals is discussed in the DWSRF annual report. The goals and accomplishments reviewed for the FY23 PER include:

Long-term goal and status:

Goal*:* Protect and Enhance Water Quality in Tennessee by ensuring the technical integrity of funded projects.

Status: TDEC is developing new standard operating procedures (SOPs), financial sufficiency processes, a new database for tracking projects, and improving integration with other TDEC programs. In addition, TDEC is working with EPA to hire a contractor to conduct a management study of their SRF programs to help TDEC update and refine their processes to ensure future effectiveness.

Short-term goal and status:

Goal*:* Manage an effective and efficient DWSRF loan program.

Status: TDEC is developing new SOPs for technical and financial review process and a streamlined contacts database to reach out to potential borrowers.

SECTION IV: PROJECT FILES REVIEWED

1. One DWSRF Base program equivalency project

Loan Reviewed	Environmental Review Determination	Loan Amount
City of Elizabethton Waterline Replacement Loan Agreement Signed: 10/19/22	Finding of No Significant Impact issued: 10/7/22	Loan Amount: $1,350,000 Loan Term: 20-year Loan Interest Rate: 1.19% Principal Forgiveness: $0

The project was eligible for DWSRF funding and followed the environmental review, Davis Bacon, American Iron and Steel (AIS), Build America, Buy America (BABA), and procurement requirements.

2. One DWSRF Base project with a disadvantaged community receiving additional subsidization.

Loan Reviewed	Environmental Review Determination	Loan Amount
City of LaFollette Waterline Replacement Loan Agreement Signed: 10/19/22	None	Loan Amount: $170,000 Loan Term: 5-year Loan Interest Rate: 0.66% Principal Forgiveness: $85,000

The project was eligible for DWSRF funding and followed the environmental review, Davis Bacon, AIS, and procurement requirements.

SECTION V: ENVIRONMENTAL BENEFITS REPORTING

FY23 Loans	Public Benefit	Total Investment
11	Improvements to public water systems promoting compliance, ensuring water supply, and protecting public health.	$46,820,111.24

TDEC updated the Office of Water State Revolving Fund (OWSRF) database in a timely fashion as required by the grant agreement. All necessary information about projects funded in FY23 was entered in the OWSRF system. TDEC is continuing its efforts to update all data fields from prior capitalization grants after projects construction periods have ended.

SECTION VI: ADDITIONAL SUBSIDIZATION AND POPULATION SERVED

	Assistance for Small Systems (<10,000)	Additional Subsidization Disbursed	Number of Projects that received Additional Subsidization
FY22 Disbursement Totals	$3,417,400	$459,500	3
FY23 Disbursement Totals	$5,600,000	$755,000	3

Additional Subsidy Assigned from Executed Loan Agreements*				
Capitalization Grant	**Grant Award Amount ($)**	**Required Subsidy (%)**	**Assigned Subsidy ($)**	**Assigned Subsidy (%)**
FY22 Base	$12,172,000	26-49%	$0	0%
FY22 BIL General Supplemental	$31,253,000	49%	$5,900,000	19%
FY22 BIL Lead Service Line Replacement	$49,243,000	49%	$0	0%
FY22 BIL Emerging Contaminants	$13,123,000	100%	$0	0%

*Data obtained from OWSRF System on September 19, 2024. This is an ongoing process; TDEC will assign additional subsidy as loan agreements are executed.

Base Additional Subsidy Requirements

The terms and conditions of the grant award require additional subsidy to borrowers of the DWSRF loan program. In addition to the disadvantaged community additional subsidy assistance that must be provided as described in Section 1452(d) of the SDWA in an amount between 12 percent and 35 percent, an additional 14 percent of the capitalization grant must be provided as additional subsidization under the 2022 Congressional Add-Sub authority to eligible borrowers. TDEC's FY22 and FY23 capitalization grants were open and making principal forgiveness disbursements at the time of this review. Region 4 will confirm that the program's additional subsidy requirements were met before closing its grants.

Bipartisan Infrastructure Law Additional Subsidy Requirements

General Supplemental

The terms and conditions of the grant award require additional subsidy to borrowers of the DWSRF loan program that meet state defined disadvantaged community criteria. As described in the Bipartisan Infrastructure Law, additional subsidy assistance must be provided in an amount of 49 percent. Tennessee's FY22 and FY23 BIL General Supplemental Capitalization Grants were open and making additional subsidy disbursements at the time of this review. Region 4 will confirm the program's additional subsidy requirements were met before closing its grant.

Lead Service Line Replacement

The terms and conditions of the grant award require additional subsidy to borrowers of the DWSRF loan program that meet state defined disadvantaged community criteria. As described in the Bipartisan Infrastructure Law (BIL), additional subsidy assistance must be provided in an amount of 49 percent. Tennessee's FY22 and FY23 BIL LSLR Capitalization Grants were open and making principal forgiveness disbursements at the time of this review. Region 4 will confirm the program's additional subsidy requirements were met before closing its grant.

Emerging Contaminants

The terms and conditions of the grant award require 100 percent additional subsidy provided to borrowers of the DWSRF EC program. States must direct at least 25 percent of these funds to disadvantaged communities OR to public water systems serving fewer than 25,000 persons. Tennessee's FY22 capitalization was open, and the state is executing loan agreements that will have additional subsidy disbursements. Region 4 will confirm that the program's additional subsidy requirements were met before closing its grant.

SECTION VII: CASH DRAWS

Draw ID Number	Draw Date	Draw Amount
23AS1448786	5/24/2023	$383.24
23AS1437532	3/13/2023	$118,492.94
23AS1414289	10/4/2022	$98,431.34

Three cash draws that occurred in the state's FY were reviewed by EPA contractors. All invoices reviewed in the selection were found to be properly made for eligible DWSRF expenditures and were appropriately recorded. No improper payments were identified.

SECTION VIII: PROGRAM HIGHLIGHTS

Program Highlight 1

The state is exploring a new database for tracking and documenting projects and streamlining its Environmental Review Approval Process.

Program Highlight 2

A SRF Management Study will be completed by an outside contractor to evaluate the overall program. The study will identify any areas of concern and provide recommendations for improvement that will be documented in a final report.

Program Highlight 3

State representatives were transparent and forthcoming with information as evidenced by their openness to recommendations. The state also was open to assistance concerning noted issues identified during the review process and was eager to work with contractors to find solutions.

SECTION IX: FINANCIAL INDICATORS

Financial Indicators Activity	2022	2023
Return on Federal Investment	129%	137%
Assistance Provided as a % of Funds Available	73%	69%
Disbursements as a % of Assistance Provided	89%	84%
Set-Aside Spending Rate	82%	67%
Uncommitted Balances	$122M	$170M

Based on EPA's financial review, EPA concludes that the TDEC DWSRF is in sound financial condition. Note: Financial indicators data was provided by OWSRF for the monitoring period ending on June 30, 2023.

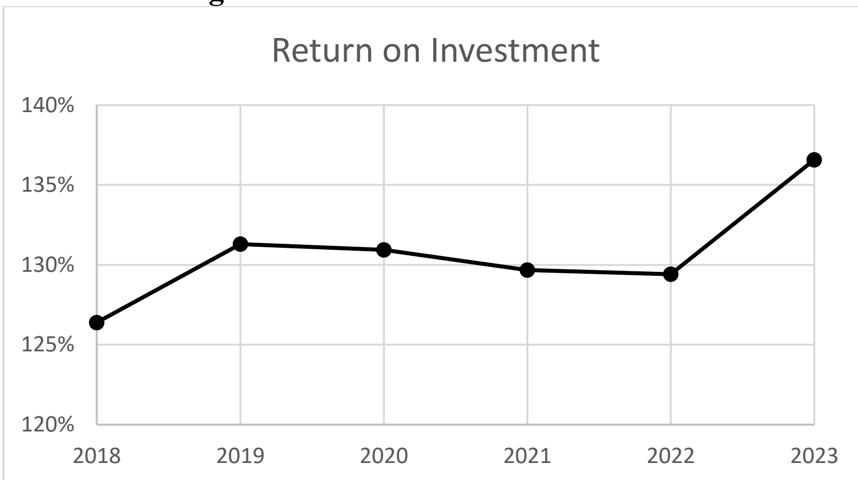
SECTION X: PROGRAM HEALTH ANALYSIS DISCUSSION

During the FY23 Annual Review, Region 4 reviewed financial indicators derived from data submitted to the SRF Data System. Based on this review, an analysis of the overall program financial health has been developed to further inform the annual review cycle.

Financial Indicators

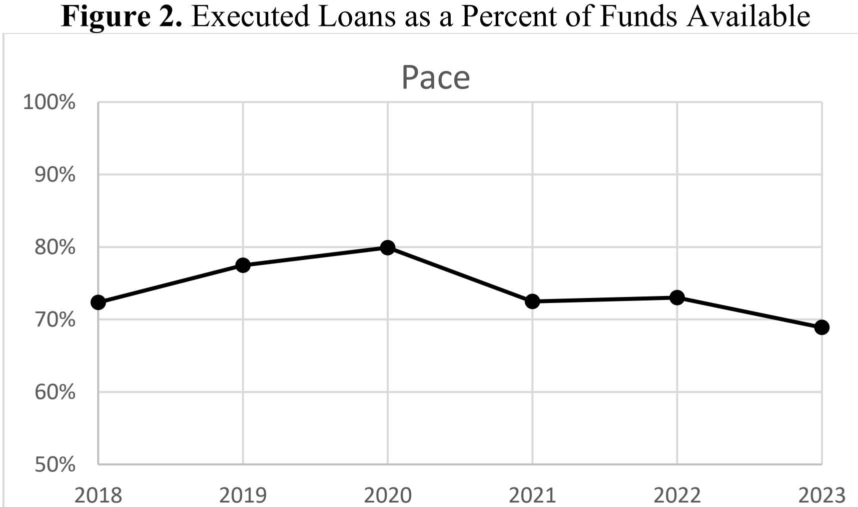
The **Federal Return on Investment** indicator shows how many dollars of assistance were disbursed to eligible borrowers for each federal dollar drawn. The State of Tennessee return on federal funds for FY23 is 137 percent. This indicates that for every federal dollar expended, approximately $1.37 of assistance is disbursed through Tennessee's DWSRF program. This indicator increased from last year, which emphasizes the success of TDEC's DWSRF program to revolve in perpetuity and maximize assistance to borrowers.

Figure 1. Federal Return on Investment



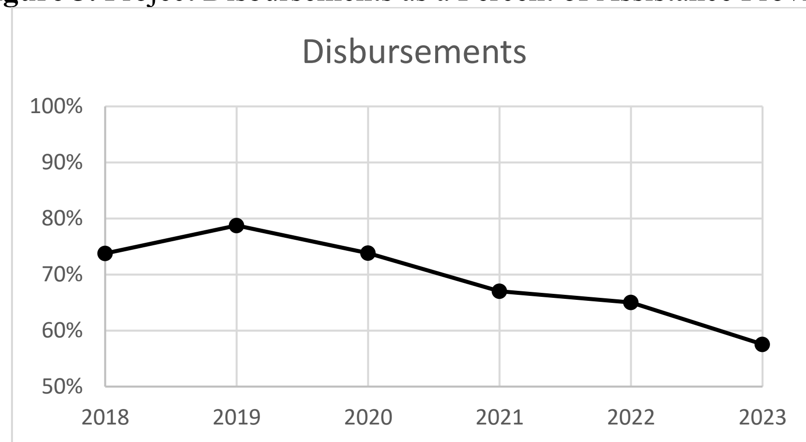
The **Executed Loans as a Percent of Funds Available** indicator measures the dollar amount of executed loan agreements to the cumulative dollar amount of funds available for loans. It is one indicator that measures the Pace of the program by gauging how quickly funds are made available to finance DWSRF projects. This indicator has a wide range of values and can exceed 100 percent for those states that have adopted an advanced loan approval approach, which makes use of the lag time between the signing of loan agreements and the disbursement of monies to complete the projects. Tennessee is proceeding to convert its DWSRF available funds into executed loans at a rate of 69 percent. TDEC's pace has declined slightly since FY22; however, this is expected with the influx or new BIL funding and implementation of new requirements. TDEC is committed towards maintaining a high pace for their program and is working to improve their processes to increase their pace.

Figure 2. Executed Loans as a Percent of Funds Available



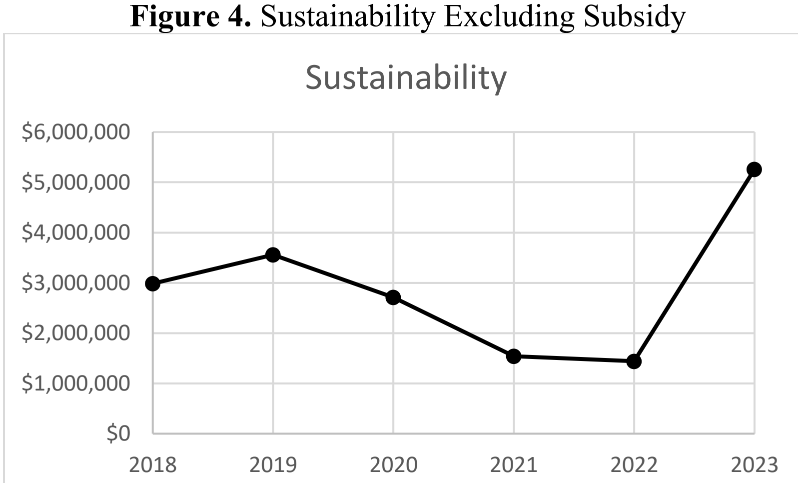
The **Project Disbursements as a Percent of Assistance Provided** indicator measures the speed at which projects are proceeding to completion. This indicator shows the relationship between loan disbursements and the total amount of funding provided. This indicator has a wide range of values, but will not exceed 100 percent, as that would indicate disbursing funds in excess of the funds committed. During FY23, Tennessee proceeded at a 58 percent rate, which has steadily decreased over the last three years. However, a decrease was anticipated by the state as various factors may have resulted in construction delays and therefore delayed invoices for costs incurred. TDEC is currently reviewing their processes to shorten the time to loan disbursements and project completion.

Figure 3. Project Disbursements as a Percent of Assistance Provided



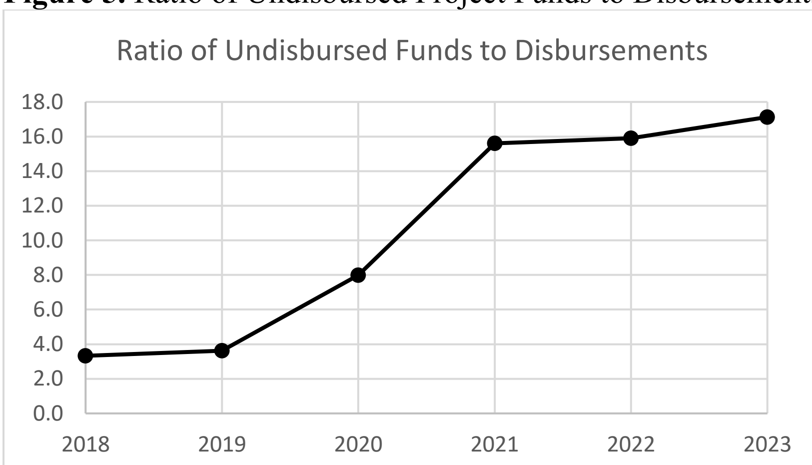
The **Sustainability Excluding Subsidy** indicator seeks to gauge how well the State's DWSRF fund is maintaining the invested capital, without making adjustments for loss of purchasing power due to inflation. Sustainability is a measure of Perpetuity, which is a measure of the amount of net earnings that has been generated by the operations of the DWSRF program. This indicator measures the dollars that have been returned to the DWSRF over and above the initial federal grants and state match deposits. These will contribute to the viability of the DWSRF and enable it to exist in perpetuity as intended by Section 1452 of the SDWA. This value should be greater than $0 (no net earnings). The Sustainability indicator for the State of Tennessee has reached over $5.2 million in SFY 2023.

Figure 4. Sustainability Excluding Subsidy



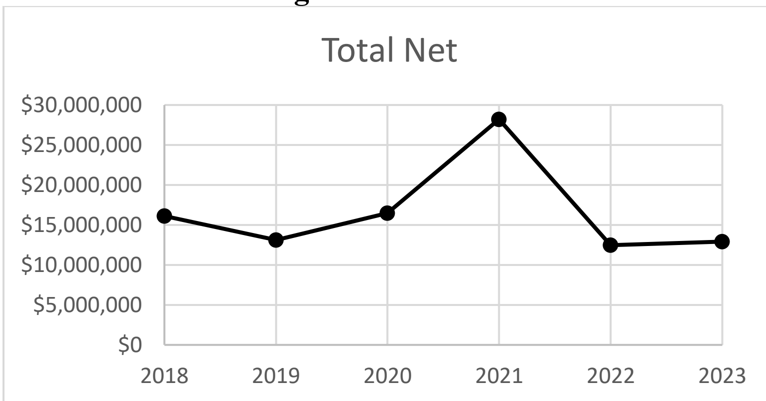
The **Ratio of Undisbursed Project Funds to Disbursements** evaluates how efficiently SRF funds are revolving by examining a program's disbursement rate over a set time period and comparing it to the amount of cash on hand. The results of this measure reflect the number of years it would take to spend the cash on hand, assuming the future disbursements are consistent with average annual disbursements over the past three years. The State of Tennessee has approximately 17.1 years' worth of undisbursed funds on hand in FY 2023. The ratio is calculated by taking the amount of all available undisbursed funds at the end of the fiscal year and determining how many years it would take to draw down the amount based on the average drawdown rate over the last three years of disbursements. The unofficial goal is to have a ratio less than 2.0, which represents having less than two years of undisbursed funds. As of June 30, 2023, Tennessee has $231,532,164 in undisbursed funds, with a three-year average annual disbursement amount of $13,517,443, equating to an undisbursed fund ration of 17.1. TDEC is continuing its efforts to decrease the undisbursed fund ratio towards the two-year goal by ensuring that the prioritization of ready-to-proceed projects and processing disbursements to eligible borrowers in a timely and expeditious manner, especially with the unprecedented levels of capitalization grant dollars through BIL.

Figure 5. Ratio of Undisbursed Project Funds to Disbursements



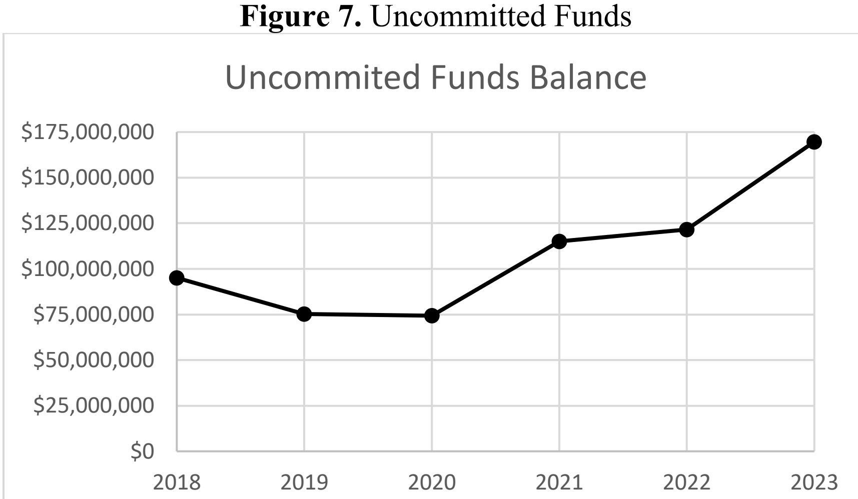
Total Net measures the extent by which internal growth is generating additional funding for new projects. It accomplishes this by taking the total cash inflows generated by ongoing loan and investment activity and subtracting out debt service payments from outstanding match and leveraged bonds. New federal capitalization grants and leveraged bond issues are also excluded from this calculation. This measure reflects the amount of new annual project funding generated solely from net repayments. Tennessee's total net is $12.9 million, which is indicative of the State continuing to grow its program.

Figure 6. Total Net



Uncommitted Funds measures the amount of funds that have not been committed to projects via loan agreements. This indicator includes all capitalization grants, state match, revolved funds, and fees deposited into the fund where applicable. This indicator has a wide range of values and can fall below $0 for those states that have adopted an advanced loan approval approach, which makes use of the lag time between the signing of the loan agreements and the disbursement of monies to completed projects. As of June 30, 2023, TDEC's DWSRF uncommitted fund balance for FY23 was $169,679,273. TDEC continuing its efforts to decrease its uncommitted funds by executing loan agreements with projects as the uncommitted funds balance has been high for several years. The state did not leverage their SRF program during FY23.

Figure 7. Uncommitted Funds



Commitments and Disbursements

Tennessee has spent considerable effort developing a marketing strategy, which maintains a pipeline of projects that are interested in utilizing SRF funding. The program consistently has a project ranking list that far exceeds the available funding; however, despite these efforts, TDEC has very rarely attained a program pace that meets the expectation of timely and expeditious use of funds. Per the Maximizing Water

Quality and Public Health Benefits by Ensuring Expeditious and Timely Use of All State Revolving Fund Resources memorandum (Expeditious and Timely Use memo*)*, the EPA reiterated the requirement that states commit funds via signed final assistance agreements within one year of receipt of funds. This applies to all funds in the SRF program, including federal capitalization grants, state match, interest earnings, and repayment. Region 4 would also like to note a concerning spike in uncommitted balances which have risen over $40M in the last year. In the FY22 PER, Region 4 recommended that TDEC take steps to reduce uncommitted funds; however, with the rise in uncommitted funds every year since 2020, it is apparent that efforts were not sufficient and more significant action will need to be taken in order to address the pace of commitment to loan agreements.

Cash disbursement trends indicate significant challenges within TDEC's DWSRF program over the last several years. Region 4 would like to highlight a rise in 2023 three-year average disbursements, from $9.9M to $13.5M, along with undisbursed funds having risen over $70M over the last year. Per the Expeditious and Timely Use memo, EPA's goal is a three-year cash-to-average-annual-disbursement ratio at or below 2.0. TDEC did not meet this metric, and further exceeded EPA's goal with a three-year cash-to-average annual disbursement ratio of 17.1 in FY23. It is therefore strongly recommended that the state take steps to improve its fund disbursements to meet the two-year metric.

Sustainability and Total Net Earnings

Program sustainability takes into account the state's ability to balance interest earnings from both loans and interest earning accounts, which grow the overall loan capacity of the SRF, with interest and principal payments made by the SRF on match bonds, which will reduce the SRF loan capacity. The goal is for the sustainability metric to be positive. The sustainability indicator shown above details a program that is growing. The view is bolstered when looking at the total net performance. Total net earnings consider the sustainability as well as principal repayments made to the SRF from borrowers and the payments by the SRF on leverage bonds. All interest and principal repayments made to the SRF continue to grow the loan capacity of the program.

While the overall performance is good, two concerns arose during review: the significant rise in interest earnings on investments, and the increasing balance of uncommitted and undisbursed funds. An SRF is expected to achieve growth, but a rapid rise in investment earnings can indicate that cash is accumulating in the SRF account very quickly or is sitting in the account long enough to accrue significant interest; however, with this being a one-time event, Region 4 is comfortable with the growth of the interest earnings and give praise to TDEC for its continued stewardship of SRF perpetuity. The second area of concern is the increasing uncommitted and undisbursed balances. Decreasing these will ultimately result in an increased program pace along with decreasing the three-year cash-to-average annual disbursement ratio.

SECTION XI: SET ASIDE PERFORMANCE

Section 1452(g)(2) of the SDWA allows the DWSRF program the option of using up to 31 percent of their capitalization grant for activities that protect sources of drinking water, enhance water systems management, and capacity development strategies. This is provided through a mechanism known as

DWSRF set asides. For the FY22 DWSRF base capitalization grant, TDEC reserved $486,880, or four percent, for set-aside activities. For the FY22 DWSRF BIL General Supplemental capitalization grant, TDEC reserved $5,800,332, or 17 percent, for set-aside activities. For the FY22 DWSRF BIL Lead Service Line Replacement, TDEC reserved $7,857,119, or 16 percent, for set-aside activities. TDEC did not reserve set-asides for their FY22 DWSRF BIL Emerging Contaminants capitalization grants. TDEC used their set-asides in the following manner:

Base

Program Administration – 4 percent
Program Administration may be four percent of the capitalization grant, $400,000, or 1/5 percent of the current valuation of the fund (whichever the state chooses) to cover the reasonable costs of administration of the DWSRF programs. TDEC obligated $486,880 for administration expenses, giving 100 percent to TDEC personnel from their FY22 Base capitalization grant. During state FY23, TDEC disbursed $0 from this set-aside.

Small System Technical Assistance – 2 percent
SDWA allows funds for technical assistance and training to help small systems build the capacity they need to provide safe drinking water. TDEC elected not to utilize this set-aside from the FY22 Base capitalization grant.

State Program Management – 10 percent
The State Program Management set-aside is generally used to support a state's Public Water System Supervision (PWSS) Program. TDEC elected not to utilize this set-aside from the FY22 Base capitalization grant.

Local Assistance – 15 percent
SDWA allows the local assistance set-aside to provide assistance, including technical and financial assistance, to public water systems as part of a capacity development strategy, safe drinking water educational events and for source water protection activities. TDEC elected not to utilize this set-aside from the FY22 Base capitalization grant.

Bipartisan Infrastructure Law – General Supplemental

Program Administration – 4 percent
Program Administration may be four percent of the capitalization grant, $400,000, or 1/5 percent of the current valuation of the fund (whichever the state chooses) to cover the reasonable costs of administration of the DWSRF programs. TDEC elected not to utilize this set-aside from the FY22 BIL GS capitalization grant.

Small System Technical Assistance – 2 percent
SDWA allows funds for technical assistance and training to help small systems build the capacity they need to provide safe drinking water. For the FY22 BIL GS capitalization grant, TDEC obligated $578,199 to support regulatory compliance and technical assistance to small communities. During state FY23,

Tennessee expended $557,146.49 from this set-aside.

State Program Management – 10 percent
The State Program Management set-aside is generally used to support a state's Public Water System Supervision (PWSS) Program. For the FY22 BIL GS capitalization grant, TDEC obligated $2,353,373 for this set-aside to support PWSS activities, including sanitary surveys, investigations, publications, and laboratory support and certification. During state FY23, Tennessee expended $2,336,040.02 from this set-aside.

Local Assistance – 15 percent
SDWA allows the local assistance set-aside to provide assistance, including technical and financial assistance, to public water systems as part of a capacity development strategy, safe drinking water educational events and for source water protection activities. For the FY22 BIL GS capitalization grant, TDEC obligated $519,744 for this set-aside to support source water protection, wellhead protection, CDP grant program development, and source water protection loan program development. During state FY23, Tennessee expended $205,080.12 from this set-aside.

Bipartisan Infrastructure Law – Lead Service Line Replacement

Program Administration – 4 percent
Program Administration may be four percent of the capitalization grant, $400,000, or 1/5 percent of the current valuation of the fund (whichever the state chooses) to cover the reasonable costs of administration of the DWSRF programs. TDEC elected to not utilize this set-aside from the FY22 BIL LSLR capitalization grant.

Small System Technical Assistance – 2 percent
SDWA allows funds for technical assistance and training to help small systems build the capacity they need to provide safe drinking water. TDEC elected not to utilize this set-aside from the FY22 BIL LSLR capitalization grant.

State Program Management – 10 percent
For State Program Management, TDEC obligated $478,093 from their FY22 BIL LSLR capitalization grant to develop a Lead and Copper Revisions for investigations, publications, compliance, and inventory framework. During FY23, TDEC expended $61,632.09 from this set-aside.

Local Assistance – 15 percent
For Local Assistance, TDEC obligated $7,379,026 from their FY22 BIL LSLR to develop Tennessee's Lead Service Line Inventory for investigations, publications, compliance, and inventory framework. During FY23, TDEC expended $45,611.62 from this set-aside.

SECTION XII: FOLLOW UP ON PRIOR YEAR PROGRAM EVALUATION REPORT

There were three EPA recommendations in the FY22 DWSRF PER.

1. EPA requests that the state evaluate different approaches and options such as utilization of cash flow modeling and increased marketing of the SRF to decrease uncommitted balances and increase program pace. The state has reported that it is short staffed but has made efforts to improve response rates to solicitation for projects. In addition, TDEC reports a significant increase in project funding requests.

   Status: TDEC has increased the number of loans awarded due to increasing demands through education, outreach, technical assistance, and other actions. TDEC continues to increase community engagement, improve project ranking list solicitation, improve internal communication, and develop a strategy for small and disadvantaged communities.

2. EPA recommends the state maintain a fully staffed programmatic and engineering team to maintain best practices and mitigate risk to the program.

   Status: TDEC has hired seven new staff since the FY22 DWSRF PER and currently has multiple open positions being recruited and interviewed. TDEC is also pursuing a contract with an outside firm to assist with site inspections and other project management related duties until all positions are filled.

3. EPA recommends the state review project AIS letters for required elements or implement a process for ensuring AIS letters submitted to borrowers follow EPA guidelines.

   Status: TDEC has retrained technical staff on the requirements for AIS requirements, but EPA Region 4 personnel noted during project file reviews that some of AIS letters missed some of the required elements.

SECTION XIII: RECOMMENDATIONS

1. EPA recommends that the TDEC evaluate ways to reduce the cash-to-average annual disbursement ratio below two years. At this time, the preeminent recommendation for doing so includes evaluating projects for readiness to proceed to construction.

2. EPA recommends TDEC implement higher salary grades and/or increase salaries to hire specialized SRF staff to help the state maintain a fully staffed programmatic and engineering team to maintain best practices and mitigate risks to the program.

3. EPA recommends that TDEC document its plan to move money into loans through IUPs.

4. EPA recommends that TDEC ensure that all relevant data for assistance agreements are consistently entered in the SRF Data System, including the associated fiscal year appropriation grant and the assigned additional subsidization, along with relevant data for local assistance set asides.

5. EPA recommends that TDEC consider having the assistance applicant's engineer provide a certification on the useful life of the infrastructure that will be financed with the SRF loan. This will provide a check on the requirement that the loan term does not exceed the useful life of the infrastructure.

6. EPA recommends that TDEC includes BABA waiver documentation in all project files for projects eligible for the design planning waiver.

7. EPA recommends that TDEC require assistance recipients to comply with the prohibition on certain telecommunication and video surveillance services or equipment in accordance with 2 CFR 200.216, which implements section 889 of Public Law 115-232, into loan agreements for equivalency projects.

8. EPA recommends that TDEC update their standard signage templates for both non-BIL base equivalency projects to meet EPA's Guidelines for Enhancing Public Awareness of SRF Assistance Agreements (2015) and BIL-funded projects to meet EPA's Guidelines for Implementing the BIL Signage Term and Condition for SRF Programs (2022).

9. EPA recommends that TDEC update their SOPs, internal guidance documents, and/or inspection checklists to list the five requirements of AIS certification letters to help better ensure all letters are accurate and complete.

10. EPA recommends that TDEC update their SOPs and/or internal guidance documents to ensure that Technical, Managerial, and Financial Capacity is completed for all DWSRF projects before receiving financial assistance, including funds for studies, planning, and design.

11. EPA recommends that TDEC continue working to ensure compliance with the requirements of the Federal Flood Risk Management Standard, including documenting the approved floodplain determination method used and public notice procedures in the environmental determination.

12. EPA recommends that TDEC demonstrate which agencies are being consulted with for each of the environmental crosscutting authorities to ensure that each of the required environmental crosscutters are being reviewed.

SECTION XIV: FINDINGS

There are no findings.

SECTION XV: STATEMENT OF COMPLIANCE WITH SRF ANNUAL REVIEW GUIDANCE

EPA Region 4 have conducted an annual review of Tennessee's Drinking Water State Revolving Fund Program for FY23 in accordance with EPA's SRF Annual Review Guidance.

Agenda Item 5c

U. S. ENVIRONMENTAL PROTECTION AGENCY
REGION 4
PROGRAM EVALUATION REPORT
OCTOBER 8, 2024

Tennessee Clean Water State Revolving Fund
State Fiscal Year 2023
July 1, 2022 – June 30, 2023

Contents

EXECUTIVE SUMMARY

This Program Evaluation Report (PER) reviews the performance of the Tennessee Department of Environment and Conservation's (TDEC) Clean Water State Revolving Fund program (CWSRF) for State of Tennessee fiscal year (FY) 2023, which runs from July 1, 2022, to June 30, 2023. The U.S. Environmental Protection Agency (EPA) is required by 40 CFR § 35.3165 to annually assess the success of TDEC's performance of activities to determine compliance with the terms of the capitalization grant agreement. In part, the EPA utilized TDEC's FY22 CWSRF Intended Use Plans (IUP) and FY23 annual report in its review.

On November 15, 2021, the President signed P.L. 117-58, the "Bipartisan Infrastructure Law (BIL), also known as the "Infrastructure Investment and Jobs Act of 2021" (IIJA) into law. EPA awarded BIL supplemental capitalization grants through the state's CWSRF program for water infrastructure projects.

The EPA Federal FY22 Base capitalization grant provided Tennessee with $16,808,000 in clean water assistance. This required a 20 percent state match of $3,361,600. When added to the CWSRF capitalization grant the total is $20,169,600.

The EPA Federal FY22 BIL General Supplemental (GS) capitalization grant provided Tennessee with $25,855,000 in clean water assistance. This required a 10 percent state match of $2,585,500. When added to the CWSRF capitalization grant the total available for assistance is $28,440,500.

The EPA Federal FY22 BIL Emerging Contaminants (EC) capitalization grant provided Tennessee with $1,358,000 in CWSRF. There is no required state match. No assistance agreements were established during FY23.

During FY23, TDEC made 12 new CWSRF loans to local governments or water and sewer authorities totaling $61,687,699. One of the metrics the EPA uses in evaluating state programs is "pace" which is defined as the cumulative amount of loans issued as a percentage of all funds available. As of June 30, 2023, the reported FY23 pace of TDEC's CWSRF program was 92 percent, a decrease from TDEC's FY22 program pace of 93 percent. The national average for FY23 is 99 percent.

The Tennessee CWSRF has been 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 TDEC and the EPA and the conditions of the capitalization grant agreement.

SECTION I: PURPOSE AND SCOPE

The EPA Region 4 began the FY23 annual review of the Tennessee CWSRF with an opening meeting on May 28, 2024. The review concluded with a closing conference on September 23, 2024. The review process was conducted as prescribed in Section 606(e) of the CWA, 40 CFR § 35.3165 and in the Annual Review Guidance issued in October 2023. The review was conducted in a hybrid approach, both virtually and in person.

The purposes of the annual review are to:

1. Evaluate the success of the state's performance in achieving goals and objectives identified in the IUP, and the state's annual report;

2. Evaluate the state's compliance with regulations, operating agreement, and capitalization grant agreement;

3. Assess the financial status and performance of the fund;

4. Review the program in accordance with EPA's SRF Annual Review Guidance;

5. Review the status of resolution of prior year PER findings; and

6. Examine and follow up on any open audit findings and recommendations.

In attendance at the opening conference for TDEC were Vena Jones, Felicia Freeman, Lacey Black, and Paula Mitchell. Attending from the EPA Region 4 were Brooke Pine, Chris Bruegge, and Jill Causse. Attending from EPA Headquarters were Kelly Tucker, Howard Rubin, and Logan Loadholtz.

During the review period, EPA Region 4 examined project files, loan agreements, any additional supporting documents, and met with ADEM staff to better understand issues and exchange information. EPA contractors, meanwhile, tested financial transactions.

At the completion of the review, a virtual exit briefing was held to review the observations made by the EPA and to clarify any outstanding issues. Attending the exit conference for TDEC were Paula Mitchell, Vena Jones, and Lacey Black. Attending from the EPA Region 4 were Johnnie Purify, Mara Lindsley, Jill Causse, Tracy Williams, Chris Bruegge, Vincent Harvey, and Ronekisha Oliver.

SECTION II: COMPLIANCE REQUIREMENTS

TDEC provided the EPA with the most recent financial audit for the year ending June 30, 2023. This audit dated December 2023, contained no findings.

TDEC is in compliance with the Disadvantaged Business Enterprise (DBE) requirement detailed in their FY22 CWSRF capitalization grant awards. TDEC's DBE participation for the most recent reporting year was 6.94 percent. TDEC provides assurances that borrowers follow the six affirmative steps for DBE participation.

TDEC is in compliance with the 15 assurances stated in the grant agreement. These assurances have their basis in 40 CFR § 35.3135.

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

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

   Status: TDEC certified this in the FY22 IUP.

2. Assurance that the state will provide an amount equal to 20 percent of base capitalization grant and 10 percent of BIL General Supplemental capitalization grant (state match) in the fund.

   Status: The FY22 base capitalization grant was $16,808,000. The 20 percent state match amount of $3,361,600 was provided through state appropriation funds. The FY22 BIL General Supplemental capitalization grant was $25,855,000. The 10 percent state match amount of $2,585,500 was provided through state appropriation funds.

3. Assurance that the state will 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 made 12 loans with local governments or water and sewer authorities totaling $61,687,699 in FY23. TDEC met this requirement.

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

   Status: The cumulative pace percentage for TDEC in FY23 was 92 percent; a decrease from TDEC's FY22 program pace of 93 percent. TDEC disbursed a total of $78,223,744 from the CWSRF in FY23.

5. Assurance that the CWSRF must be utilized 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: TDEC funded wastewater and stormwater projects with qualified local governments or water and sewer authorities to meet this requirement.

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

   Status: TDEC certified this in the FY22 IUPs and FY23 Annual Report.

7. Assurance that 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 FY23 annual report, under the provisions of the operating agreement/conditions of their grant, the state certified compliance with other federal authorities.

8. Assurance that 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, 2023, were tested by EPA contractors, and were made for eligible costs incurred in accordance with 40 CFR § 35.3160.

9. Assurance that the state is required to establish fiscal control and accounting procedures that are sufficient to ensure 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 utilize 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 FY23 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. Assurance that 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: TDEC has complied with this requirement via a condition in the loan agreement for borrowers.

11. Assurance that the state will provide 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 FY23 annual report for TDEC's CWSRF program was due to EPA on September 30, 2023. Prior to the September 30, 2023, due date, TDEC requested an extension for their annual report ending June 30, 2023, shifting their due date to October 30, 2023. When the extended due date was not met, EPA Region 4 and TDEC negotiated two different estimated submittal dates, *those were January 1, 2024, and March 1, 2024, neither of which were met. The report, which was received on March 19, 2024, contained adequate and accurate information regarding program implementation.*

12. Assurance that the state will 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: TDEC has a NEPA-like state environmental review process (SERP) which was approved by the Region 4 Regional Administrator. TDEC has documented its assurances that it will conduct environmental reviews for all projects in its Operating Agreement. Two CWSRF projects were reviewed for compliance with the SERP in the context of the FY23 PER. Based on the available project documentation, EPA determined that the environmental reviews carried out for both projects were in compliance with the SERP.

13. Assurance that the CWSRF will only provide assistance to projects that are consistent with any plans developed under Sections 205(j), 208, 303(e), 319 and 320 of the CWA, regarding water quality management planning.

    Status: In its Operating Agreement, TDEC provides an assurance that CWSRF assistance will only be provided to projects that are consistent with the water quality management planning activities developed under Sections 205(j), 208, 303(e), 319, and 320 of the CWA. TDEC is in compliance with this requirement.

14. Assurance that the state shall submit a schedule that reflects, by quarters, the estimated disbursements from the capitalization 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 EPA and the state to jointly develop and maintain a forecast of cash draws.

    Status: TDEC complied with this regulation in the FY22 IUPs for the Clean Water Base and Clean Water BIL General Supplemental allotments.

15. Assurance that the state will 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: TDEC's FY22 IUPs were provided to EPA and included repayments and interest earnings *in the amounts available for assistance.*

SECTION III: PROGRAM GOALS

TDEC has a number of long-term and short-term goals in their IUPs. EPA evaluated one long-term and one short-term goal. TDEC is working toward meeting each of the goals evaluated. TDEC's status in meeting these goals is discussed in the CWSRF annual report. The goals and accomplishments reviewed for the FY23 Program Evaluation Report, include:

Long-term goal and status:

Goal: Provide local governments with low-cost financial assistance by ensuring that funds are obligated in a timely manner.

Status: Fiscal responsibilities are coordinated with TDEC, the Comptroller's Office and the Department of Finance and Administration to ensure appropriate internal controls and proper accounting procedures. Additionally, TDEC has revised the operating budget, conducted an internal audit, and completed end of year fiscal reporting. Development of a new database for tracking funds and project progress is ongoing.

Short-term goal and status:

Goal: Maximize funds available through cooperation with EPA Region 4.

Status: TDEC is revising their IUP format for efficiency and have an ongoing innovative pilot project strategy to strengthen and grow SRF projects. Additionally, the proposed call order will focus on the completion and implementation of a Management Study of the TDEC CWSRF (and DWSRF) program that will identify ideas and options for improvement with a focus on identifying actions or steps to streamline the loan application process and improve loan material review and execution.

SECTION IV: PROJECT FILES REVIEWED

1. One CWSRF Base equivalency project

Loan Reviewed	Environmental Review Determination	Loan Amount
Town of Smyrna Inflow and Infiltration Correction Loan Agreement Signed: 7/27/22	Categorical Exclusion issued: 1/27/22	Loan Amount: $800,000 Loan Term: 20-year Loan Interest Rate: 1.92% Principal Forgiveness: $0

The project was eligible for CWSRF funding and followed the environmental review, Davis Bacon, American Iron and Steel (AIS), Build America, Buy America (BABA), and procurement requirements.

2. One CWSRF Base Project with a disadvantaged community receiving additional subsidization.

Loan Reviewed	Environmental Review Determination	Loan Amount
City of Westmoreland Wastewater Treatment Plant Improvements Loan Agreement Signed: 7/22/21	Finding of No Significant Impact issued: 9/12/19	Loan Amount: $1,096,445 Loan Term: 20-year Loan Interest Rate: 2.66% Principal Forgiveness: $219,289

The project was eligible for CWSRF funding and followed the environmental review, Davis Bacon, AIS, BABA, and procurement requirements.

SECTION V: ENVIRONMENTAL BENEFITS REPORTING

FY23 Loans	Public Benefit	Total Investment
12	Assistance to wastewater and nonpoint source projects improving water quality	$61,687,699

TDEC updated the Office of Water State Revolving Fund (OWSRF) database as required by the grant agreement in a timely fashion. All necessary information about projects funded in FY23 was entered into the OWSRF system. Some additional subsidy information for the projects were not linked properly to capitalization grants in the database.

SECTION VI: GREEN PROJECT RESERVE

FY23 Projects	Public Benefit	Total Investment
5	Green infrastructure, water or energy efficiency improvements, or other environmentally innovative activities	$26,082,000

The FY22 Capitalization Grant Terms and Conditions require the recipient to make a timely and concerted good faith solicitation for projects that address green infrastructure, water or energy efficiency improvements or other environmentally innovative activities.

Additionally, the recipient agrees to include in its IUPs such qualified projects, or components of projects, that total an amount at least equal to 10 percent of its capitalization grant.

SECTION VII: ADDITIONAL SUBSIDIZATION AND POPULATION SERVED

	Assistance for Small Systems (<10,000)	**Additional Subsidization Disbursed**	**Number of Projects that received Additional Subsidization**
FY22 Disbursement Totals	$30,815,291	$1,000,000	3
FY23 Disbursement Totals	$31,596,445	$4,465,689	4

Additional Subsidy Assigned from Executed Loan Agreements*				
Capitalization Grant	Grant Award Amount ($)	Required Subsidy (%)	Assigned Subsidy ($)	Assigned Subsidy (%)
FY22 Base	$16,808,000	20-40%	$0	0%
FY22 BIL General Supplemental	$25,855,000	49%	$0	0%
FY22 BIL Emerging Contaminants	$1,358,000	100%	$0	0%

*Data obtained from OWSRF System on September 20, 2024. This is an ongoing process; TDEC will assign additional subsidy as loan agreements are executed.

Base Additional Subsidy Requirements

The terms and conditions of the grant award allow additional subsidy to borrowers of the CWSRF loan program. In addition to the 10-30 percent additional subsidy that states are required to provide as described in the Clean Water Act and as amended by the Bipartisan Infrastructure Law, an additional 10 percent of the capitalization grant must be provided as additional subsidization under the FY22 Congressional Add-Sub authority to eligible borrowers. Tennessee's FY22 and FY23 Capitalization Grants were open and making principal forgiveness disbursements at the time of this review. Region 4 will confirm the state's additional subsidy requirements were met before closing its grant.

Bipartisan Infrastructure Law Additional Subsidy Requirements

General Supplemental

The terms and conditions of the grant award require additional subsidy to borrowers of the CWSRF loan program that meet state defined disadvantaged community criteria. As described in the Bipartisan Infrastructure Law, additional subsidy assistance must be provided in an amount of 49 percent.

Tennessee's FY22 and FY23 Capitalization Grants are open and making additional subsidy disbursements at the time of this review. Region 4 will confirm the program's additional subsidy requirements were met before closing its grant.

Emerging Contaminants

The terms and conditions of the grant award require 100 percent additional subsidy provided to borrowers of the CWSRF EC program. States must direct at least 25 percent of these funds to disadvantaged communities OR to public water systems serving fewer than 25,000 persons. Tennessee's FY22 capitalization grant was open, and the state is executing loan agreements that will have additional subsidy disbursements. Region 4 will confirm that the program's additional subsidy requirements were met before closing its grants.

SECTION VIII: CASH DRAWS

Draw ID Number	Draw Date	Draw Amount
23AS1450684	6/5/2023	$7,776.33

One cash draw was reviewed by EPA contractors. All invoices reviewed in the selection were found to be eligible CWSRF expenditures and were appropriately recorded. No improper payments were identified.

SECTION IX: PROGRAM HIGHLIGHTS

Program Highlight 1

The state is exploring a new database for tracking and documenting projects and streamlining its Environmental Review Approval Process.

Program Highlight 2

A SRF Management Study will be completed by an outside contractor to evaluate the overall program. The study will identify any areas of concern and provide recommendations for improvement that will be documented in a final report.

Program Highlight 3

State representatives were transparent and forthcoming with information, as evidenced by their openness to recommendations. The state was open to assistance concerning noted issues identified during the review process and they were eager to work with contractors to find solutions.

SECTION X: FINANCIAL INDICATORS

Financial Indicators Activity	2022	2023
Return on Federal Investment	274%	285%
Assistance Provided as a % of Funds Available	93%	92%
Disbursements as a % of Assistance Provided	88%	90%
Uncommitted Balances	$161M	$211M

Based on EPA's financial review, EPA concludes that the TDEC CWSRF is in sound financial condition. Note: Financial indicators data provided by the OWSRF report for monitoring period ending on June 30, 2023.

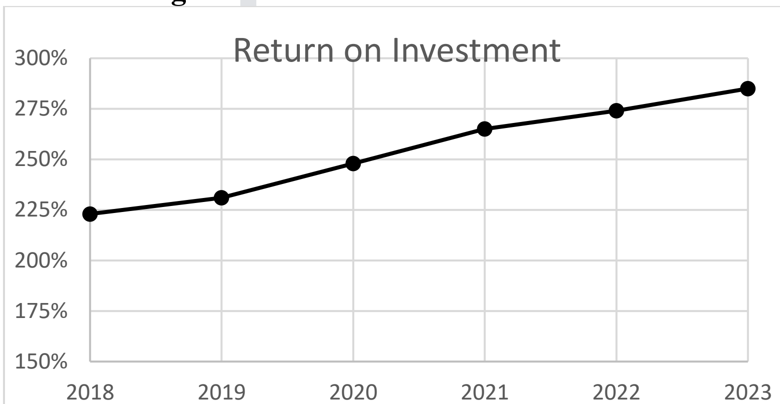
SECTION XI: PROGRAM HEALTH ANALYSIS DISCUSSION

During the FY23 Annual Review, Region 4 reviewed financial indicators derived from data submitted to the SRF Data System. Based on this review, an analysis of the overall program financial health has been developed to further inform the annual review cycle.

Financial Indicators

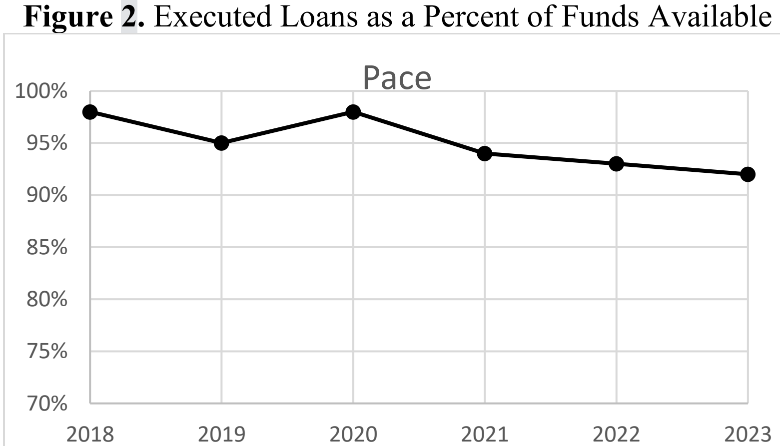
The **Federal Return on Investment** indicator shows how many dollars of assistance were disbursed to eligible borrowers for each federal dollar drawn. The State of Tennessee return rate on federal funds for FY23 is 285 percent. This indicates that for every federal dollar expended, approximately $2.85 of assistance is disbursed through Tennessee's CWSRF program. This indicator has been over 200 percent for the last three years emphasizing the success of TDEC's CWSRF program to revolve in perpetuity and maximize assistance to borrowers.

Figure 1. Federal Return on Investment



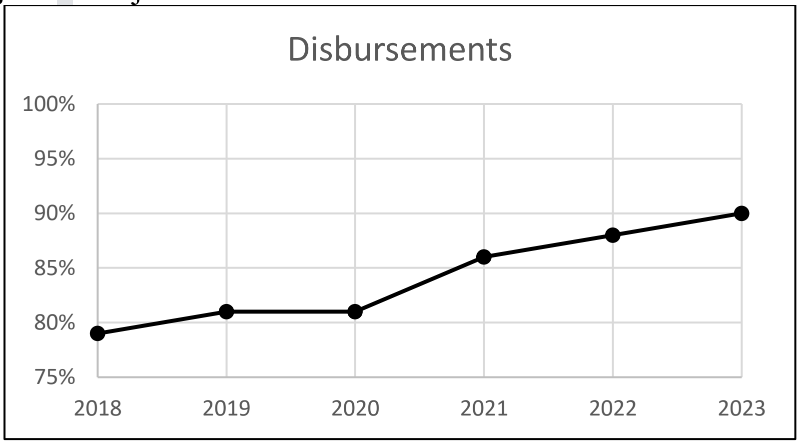
The **Executed Loans as a Percent of Funds Available** indicator measures the dollar amount of executed loan agreements to the cumulative dollar amount of funds available for loans. It is one indicator that measures the pace of the program by gauging how quickly funds are made available to finance CWSRF projects. This indicator has a wide range of values and can exceed 100 percent for those states that have adopted an advanced loan approval approach, which makes use of the lag time between the signing of loan agreements and the disbursement of monies to complete the projects. Tennessee is proceeding to convert its CWSRF available funds into executed loans at a rate of 92 percent. TDEC's pace has declined slightly since FY21 and is below the national average of 99 percent. EPA held discussions with TDEC during the onsite visit to identify ways to increase the pace to ensure continued successful commitment of executed loan agreements for the program.

Figure 2. Executed Loans as a Percent of Funds Available



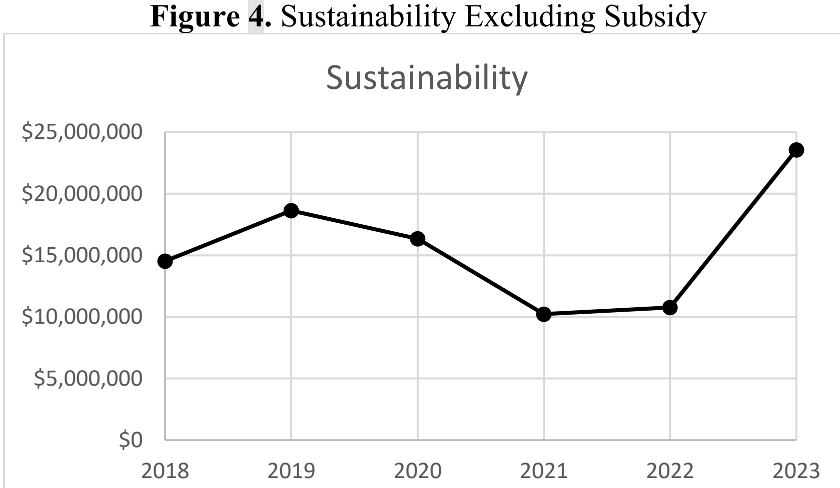
The **Project Disbursements as a Percent of Assistance Provided** indicator measures the speed at which projects are proceeding to completion. This indicator shows the relationship between loan disbursements and the total amount of funding provided. This indicator has a wide range of values but will not exceed 100 percent as that would indicate disbursing funds in excess of the funds committed. During FY23, Tennessee proceeded at a disbursement rate of 90 percent, which is an increase from the FY22 disbursement rate of 88 percent.

Figure 3. Project Disbursements as a Percent of Assistance Provided



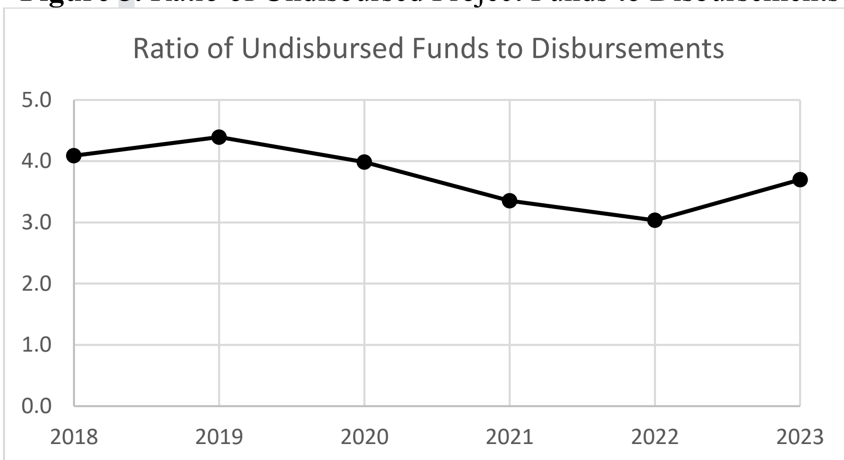
The **Sustainability Excluding Subsidy** indicator seeks to gauge how well the State's CWSRF fund is maintaining the invested capital, without making adjustments for loss of purchasing power due to inflation. Sustainability is a measure of Perpetuity, which is a measure of the amount of net earnings that has been generated by the operations of the CWSRF program. This indicator measures the dollars that have been returned to the CWSRF over and above the initial Federal grants and State match deposits. These will contribute to the viability of the CWSRF and enable it to exist in perpetuity as intended by Title VI of the CWA. This value should be greater than $0 (no net earnings). The Sustainability indicator for the State of Tennessee has reached over $24 Million in FY23.

Figure 4. Sustainability Excluding Subsidy



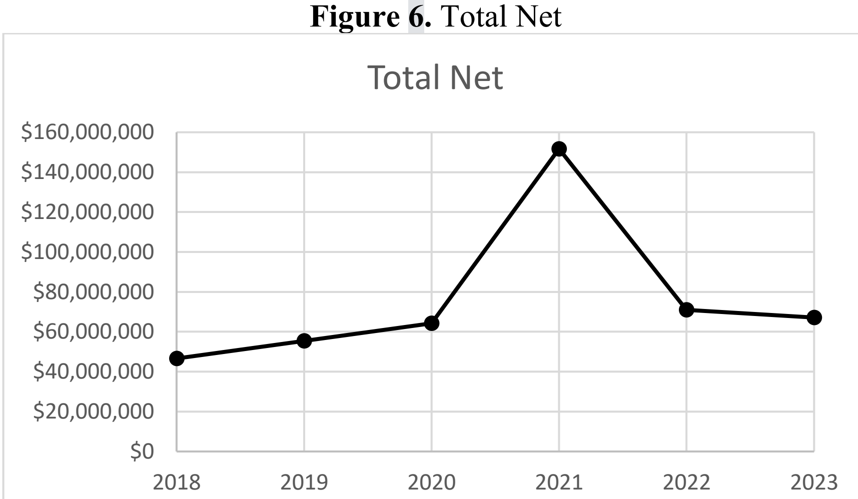
The **Ratio of Undisbursed Project Funds to Disbursements** evaluates how efficiently SRF funds are revolving by examining a program's disbursement rate over a set time period and comparing it to the amount of cash on hand. The results of this measure reflect the number of years it would take to spend the cash on hand, assuming the future disbursements are consistent with average annual disbursements over the past three years. The State of Tennessee has approximately 3.7 years' worth of undisbursed funds on hand in FY23. The ratio is calculated by taking the amount of all available undisbursed funds at the end of the fiscal year and determining how many years it would take to draw down the amount based on the average drawdown rate over the last three years of disbursements. The unofficial goal is to have a ratio less than 2.0 which represents having less than two years of undisbursed funds. As of June 30, 2023, Tennessee has $450,553,558 in undisbursed funds with a three-year average annual disbursement amount of $121,828,533 equating to an undisbursed fund ratio of 3.7. TDEC is continuing its efforts to decrease the undisbursed fund ratio towards the two-year goal by ensuring the prioritization of ready to proceed projects and processing disbursements to eligible borrowers in a timely and expeditious manner.

Figure 5. Ratio of Undisbursed Project Funds to Disbursements



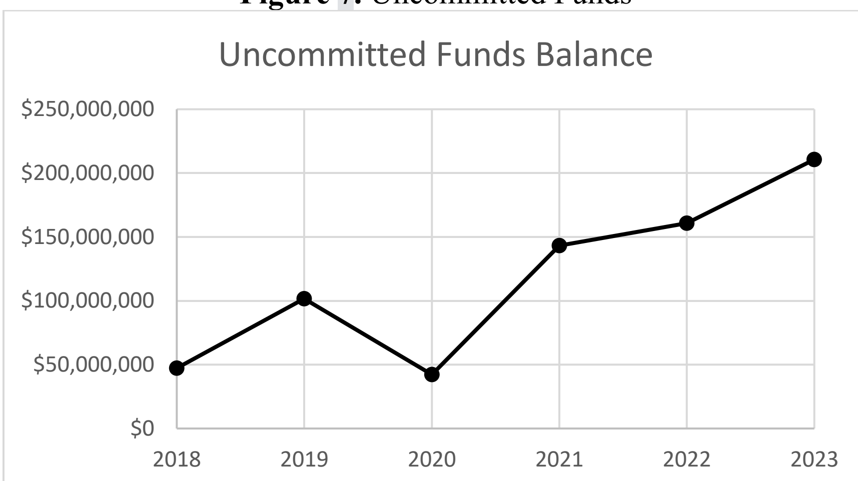
Total Net measures the extent by which internal growth is generating additional funding for new projects. It accomplishes this by taking the total cash inflows generated by ongoing loan and investment activity and subtracting out debt service payments from outstanding match and leveraged bonds. New federal capitalization grants and leveraged bond issues are also excluded from this calculation. This measure reflects the amount of new annual project funding generated solely from net repayments. Tennessee's total net for FY23 is $67 million, which is a slight decrease from FY22 total net of $71 million.

Figure 6. Total Net



Uncommitted funds measure the amount of funds that have not been committed to projects via loan agreements. This indicator includes all capitalization grants, state match, revolved funds, and fees deposited into the fund where applicable. This indicator has a wide range of values and can fall below $0 for those states that have adopted an advanced loan approval approach, which makes use of the lag time between the signing of loan agreements and the disbursement of monies to complete projects. As of June 30, 2023, TDEC's CWSRF uncommitted fund balance for FY23 was $210,660,010, indicating that there remains a high balance of uncommitted funds. TDEC's uncommitted funds for FY23 increased from FY22 uncommitted balance of $160,897,693. TDEC stated that it is continuing its efforts to decrease its uncommitted funds by executing loan agreements for projects. TDEC did not leverage the SRF program during FY23.

Figure 7. Uncommitted Funds



Commitments and Disbursements

Tennessee has spent considerable effort in developing a marketing strategy which maintains a pipeline of projects that are interested in utilizing SRF funding. The program consistently has a project ranking list that far exceeds the available funding; however, since at least 2020, TDEC's CWSRF program has experienced significant challenges in processing loan applications and signing loan agreements. This is reflected in the uncommitted balances and falling pace seen in the charts above. While the program was near a 100% pace in 2020, since that time it has fallen year over year, currently sitting at 92 percent. Region 4 would also like to note a concerning spike in uncommitted balances, which have risen nearly $50 Million in the last year. Per the Maximizing Water Quality and Public Health Benefits by Ensuring Expeditious and Timely Use of All State Revolving Fund Resources memorandum *(*Expeditious and Timely Use memo*),* the EPA reiterated the requirement that states commit funds via signed final assistance agreements within one year of receipt of funds. This applies to all funds in the SRF program, including federal capitalization grants, state match, interest earnings, and repayment. In the FY22 PER, Region 4 recommended that TDEC take steps to reduce uncommitted funds; however, with the rise in uncommitted funds, it is apparent that efforts were not sufficient and more significant action will need to be taken to address the pace of commitment to loan agreements.

Region 4 would like to note that disbursements are not displaying the same challenges but have room for improvement. Per the Expeditious and Timely Use memo, the EPA will gauge disbursement performance as adequate when the three-year cash-to-average-annual-disbursement ratio is at or below two years. While Tennessee did not meet this metric, a three-year cash-to-average-annual-disbursement ratio of 3.7 shows a program holding steady. It is recommended that the state take steps to improve its fund disbursements to meet the two-year metric.

Sustainability and Total Net Earnings

Program sustainability takes into account the state's ability to balance interest earnings from both loans and interest earning accounts, which grow the overall loan capacity of the SRF, with interest and principal payments made by the SRF on match bonds, which will reduce the SRF loan capacity. The goal is for the sustainability metric to be positive. The sustainability indicator shown above details a program that is growing. The view is bolstered when looking at the total net performance. Total net earnings consider the sustainability as well as principal repayments made to the SRF from borrowers and the payments by the SRF on leverage bonds. All interest and principal repayments made to the SRF continue to grow the loan capacity of the program.

While the overall performance is good, two concerns arose during review: the significant rise in interest earnings on investments, and the increasing balance of uncommitted and undisbursed funds. An SRF is expected to achieve growth, but a rapid rise in investment earnings can indicate that cash is accumulating in the SRF account very quickly or is sitting in the account long enough to accrue significant interest; however, with this being a one-time event, Region 4 is comfortable with the growth of the interest earnings and give praise to TDEC for its continued stewardship of SRF perpetuity. The second area of concern is the increasing uncommitted and undisbursed balances. Decreasing these will ultimately result in an increased program pace along with decreasing the three-year cash-to-average annual disbursement ratio.

SECTION XII: FOLLOW UP ON PRIOR YEAR PROGRAM EVALUATION REPORT

There were three EPA recommendations in the FY22 CWSRF PER.

1. EPA recommends that TDEC work to reduce the balance of uncommitted funds. TDEC's uncommitted balance increased from $143M to $161M in FY22.

   Status: TDEC has increased the number of loans awarded by increasing demand through education, outreach, technical assistance, and other actions; however, TDEC's uncommitted funds balance in FY23 has increased to $210M. TDEC continues to increase community engagement, improve project ranking list solicitation, improve internal communication, and develop a strategy for small and disadvantaged communities.

2. EPA recommends that TDEC maintains a fully staffed programmatic and engineering team to maintain best practices and mitigate risk to the program.

   Status: TDEC has hired seven new staff since the FY22 CWSRF PER and currently has multiple open positions being recruited and interviewed. TDEC is also pursuing a contract with an outside firm to assist with site inspections and other project management related duties until all positions are filled.

3. EPA recommends that TDEC implements a process or Standard operating Procedure (SOP) to streamline AIS letter review and ensure AIS letters submitted to borrowers follow EPA guidelines.

   Status: TDEC has retrained technical staff on the requirements for AIS requirements, but EPA Region 4 personnel noted during project file reviews that some AIS letters missed some of the required elements.

SECTION XIII: RECOMMENDATIONS

1. EPA recommends that the Tennessee Department of Environment and Conservation evaluate ways to reduce the cash-to-average annual disbursement ratio below two years. At this time, the preeminent recommendation for doing so includes evaluating projects for readiness to proceed to construction.

2. EPA recommends TDEC implement higher salary grades and/or increase salaries to hire specialized SRF staff to help the state maintain a fully staffed programmatic and engineering team to maintain best practices and mitigate risks to the program.

3. EPA recommends that TDEC document its plan to move money into loans through IUPs.

4. EPA recommends that TDEC ensure that all relevant data for assistance agreements are consistently entered in the OWSRF database, including the associated fiscal year appropriation grant and the assigned additional subsidization.

5. EPA recommends that TDEC consider having the assistance applicant's engineer provide a certification on the useful life of the infrastructure that will be financed with the SRF loan. This will provide a check on the requirement that the loan term does not exceed the useful life of the infrastructure.

6. EPA recommends that TDEC utilize a Green Project Reserve (GPR) Determination checklist when processing applications to assist with ensuring the correct loan amounts and GPR category are being assigned and entered into the OWSRF database.

7. EPA recommends that TDEC includes BABA waiver documentation in all project files for projects

eligible for the design planning waiver.

8. EPA recommends that TDEC require assistance recipients to comply with the prohibition on certain telecommunication and video surveillance services or equipment in accordance with 2 CFR 200.216, which implements section 889 of Public Law 115-232, into loan agreements for equivalency projects.

9. EPA recommends that TDEC states the assistant recipient's revenue repayment source in the financial analysis approval letter.

10. EPA recommends that TDEC update their standard signage templates for both non-BIL base equivalency projects to meet EPA's Guidelines for Enhancing Public Awareness of SRF Assistance Agreements (2015) and BIL-funded projects to meet EPA's Guidelines for Implementing the BIL Signage Term and Condition for SRF Programs (2022).

11. EPA recommends that TDEC update their Standard Operating Procedures, internal guidance documents, and/or inspection checklists to list the five requirements of American Iron and Steel certification letters to help better ensure all letters are accurate and complete.

12. EPA recommends that TDEC continue working to ensure compliance with the requirements of the Federal Flood Risk Management Standard, including documenting the approved floodplain determination method used and public notice procedures in the environmental determination.

13. EPA recommends that TDEC demonstrate which agencies are being consulted with for each of the environmental crosscutting authorities to ensure that each of the required environmental crosscutters are being reviewed.

SECTION XIV: FINDINGS

There are no findings.

SECTION XV: STATEMENT OF COMPLIANCE WITH SRF ANNUAL REVIEW GUIDANCE

EPA Region 4 has conducted an annual review of Tennessee's Clean Water State Revolving Fund Program for FY23 in accordance with EPA's SRF Annual Review Guidance.

Agenda Item 6a

TENNESSEE COMPTROLLER OF THE TREASURY

JASON E. MUMPOWER
Comptroller

To: Members of the Tennessee Local Development Authority Audit Committee

From: Sandi Thompson
Director, Division of State Government Finance (SGF)

Date: May 9, 2025

Subject: Risk Assessments

Please see the attached management risk assessments for SGF and the Division of Water Resources. 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 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 to:

1. Provide accountability for meeting program objectives,
2. Promote operational efficiency and effectiveness,
3. Improve reliability of financial statements,
4. Strengthen compliance with laws, regulations, rules, and contracts and grant agreements, and
5. Reduce the risk of financial or other asset losses due to fraud, waste, and abuse.

Please let me know if you need any additional information in this regard.

Agenda Item #9

TLDA Audit Committee						
Responsbilities Calendar						
6/23/2025						
	Responsibilities	**Documentation**	**Presented By**	**Agenda Reference**	**AC Meeting Date**	**Notes**
1	Review significant accounting and reporting standards.	Minutes Discussion	Alicia West	Item #4	7/22/2024	
2	Review financial statements and comprehensive annual financial report.	Minutes Discussion	Tabitha Furlong, State Audit	Item #3	7/22/2024	
3	Review with management the adequacy of internal controls for compliance with policies, plans, procedures, laws, and regulations.	FY23 SLF & TDEC Risk Assessments	Sandi Thompson	Item #6	7/22/2024	
4	Understand the scope of external auditors' review of internal control.	June 30, 2023 Audit Report	Tabitha Furlong, State Audit	Item #3	7/22/2024	
5	Review processes in place to assess risk, including fraud risk, which shall include a review of management's risk assessment process, in the agency.	FY23 SLF & TDEC Risk Assessments	Sandi Thompson	Item #6	7/22/2024	
6	Inquire of management and auditors about significant risks and how those risks are managed.	FY23 SLF & TDEC Risk Assessments	Sandi Thompson	Item #6	7/22/2024	
7	Review reports issued by external auditors.	Minutes Discussion	Tabitha Furlong, State Audit	Item #3	7/22/2024	Comptroller's Audit Reports
8	Ensure management has taken appropriate action on audit recommendations made by the auditors.	Minutes Discussion	N/A	Item #3	7/22/2024	No audit recommendations
9	Discuss the proposed scope and approach of the external audit.	June 30, 2023 Audit Report	Tabitha Furlong, State Audit	Item #3	7/22/2024	Comptroller's Audit Reports
10	Discuss the results of the audit with representatives of the Comptroller of the Treasury, including any difficulties encountered during the course of the audit.	Minutes Discussion	Tabitha Furlong, State Audit	Item #3	7/22/2024	
11	Encourage external auditors to discuss any issues of concern with the audit committee.	Minutes Discussion	Tabitha Furlong, State Audit	Item #3	7/22/2024	No issues or concerns
12	Immediately report any fraud to the Comptroller of the Treasury's office.	Minutes Discussion	Sandi Thompson	Item #7	7/22/2024	
13	Communicate to management their responsibility for preventing, detecting, and reporting fraud, waste and abuse, and reporting any instances of fraud, waste, and abuse to the audit committee and the Comptroller of the Treasury.	Minutes Discussion	Sandi Thompson	Item #7	7/22/2024	
14	Ensure procedures exist for the receipt, retention, and treatment of complaints about accounting, internal controls, or auditing matters.	Minutes Discussion	Sandi Thompson	Item #8	7/22/2024	
15	Regularly update the board about committee activities and make appropriate recommendations.	Report given at each board meeting following AC	Treasurer Lillard	N/A	7/22/2024	Delivered by Treasurer at the TLDA Board meeting
16	Periodically review and amend, as necessary, the audit committee charter.	Exhibit- 4/15/2019 audit committee charter	Earle Pierce	Tab 2a	6/27/2019	
17	Review management's assertion that internal controls are effective and adequate.	FY23 SLF & TDEC Risk Assessments	Sandi Thompson	Item #6	7/22/2024	
18	Evaluate whether management is setting the appropriate 'control culture' and 'tone at the top' by communicating the importance of internal controls and risk management.	Minutes Discussion	Sandi Thompson	Item #7	7/22/2024	
19	Provide a mechanism for staff to report any suspected fraud, abuse or other complaints related to operations to the audit committee.	Minutes Discussion	Sandi Thompson	Item #8	7/22/2024	