

Washington State Auditor's Office

Financial Statements Audit Report

**Department of Ecology
Water Pollution Control State Revolving Fund**

Audit Period
July 1, 2012 through June 30, 2013

Report No. 1012022

Issue Date
June 2, 2014



**Washington State Auditor
Troy Kelley**

Independence • Respect • Integrity



Washington State Auditor Troy Kelley

June 2, 2014

Maia Bellon, Director
Department of Ecology
Water Quality Program
Olympia, Washington

Report on Financial Statements

Please find attached our report on the Department of Ecology Water Pollution Control State Revolving Fund's financial statements.

We are issuing this report in order to provide information on the Department's State Revolving Fund's financial condition.

Sincerely,

A handwritten signature in cursive script that reads "Troy X. Kelley".

TROY KELLEY
STATE AUDITOR

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Department of Ecology
Water Pollution Control State Revolving Fund
July 1, 2012 through June 30, 2013**

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Schedule of Audit Findings and Responses

State of Washington Department of Ecology Water Pollution Control State Revolving Fund July 1, 2012 through June 30, 2013

1. The Department's internal controls over financial statement preparation are inadequate to ensure accurate and complete reporting for the Water Pollution Control State Revolving Fund.

Background

The Environmental Protection Agency (EPA) has designated the Department as the Washington State administrator of the Water Pollution Control State Revolving Fund (SRF). The SRF account was established to provide financial assistance in the form of low-interest loans to local governments and tribes for high priority water quality projects. The program is funded annually by EPA with a 20 percent state match, loan repayments and interest earned on investments.

The Department is responsible for designing and following internal controls that provide reasonable assurance regarding the reliability of financial reporting. Our audit identified a significant deficiency in internal controls over financial reporting that affects the Department's ability to produce accurate and complete financial statements for the SRF account.

Description of Condition

During our audit, we identified the following deficiencies in internal controls, when taken together represent a significant deficiency:

- The key employee responsible for compiling the financial statements left the Department. The remaining accounting staff did not have adequate technical knowledge to prepare the statements in conformity with Generally Accepted Accounting Principles (GAAP).
- The Department did not have an employee, independent of the preparation process, with the experience and technical knowledgeable to review the financial statements for accuracy and completeness.

Cause of Condition

The Department has not dedicated adequate resources to financial statement preparation or the development of effective internal control policies and procedures.

Effect of Condition

The Department's 2013 financial statements submitted for SRF account audit were not prepared in accordance with GAAP and contained errors. We received a total of three sets of financial statements from the Department to audit. We identified the following errors:

- The Department did not implement Governmental Accounting Standards Board Statement No. 63, relating to the presentation of net position when preparing its financial statements as required by the Governmental Accounting Standards Board.
- The liabilities on the Statement of Net Position were incorrectly totaled, resulting in the liabilities being understated in the amount of \$7.3 million.

All the errors were eventually corrected.

Recommendation

We recommend the Department dedicate the necessary staff resources, technical training and oversight to ensure:

- The Department SRF's financial statements are accurately prepared in accordance with GAAP.
- Someone knowledgeable of financial reporting requirements and independent of the financial statement preparation process performs a thorough review of the SRF's financial statement and supporting schedules to ensure they are accurate, complete and presented in accordance with GAAP.

Department's Response

The Department of Ecology recognizes the importance of its Senior Financial Advisor position, including the assigned duty of the preparation of the Water Pollution Control Revolving Account financial statements. Recruiting for a qualified replacement for this position began immediately upon the resignation of the incumbent. We have completed the screening process and have selected a qualified replacement. The new Senior Financial Advisor will fill the position on or before July 1, 2014.

Auditor's Remarks

We appreciate the Department's commitment to monitor and improve its internal control processes for the SRF account. We look forward to working with the Department on this issue and will follow up on it during the next audit.

Applicable Laws and Regulations

Revised Code of Washington, Section 43.09 gives SAO the authority to provide audit services. SAO's responsibility is to express an opinion on the financial statements audit conducted in accordance with the 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.

Government Auditing Standards, December 2011 Revision, paragraph 4.23, states:

4.23 When performing GAGAS financial audits, auditors should communicate in the report on internal control over financial reporting and compliance, based upon the work performed, (1) significant deficiencies and material weaknesses in internal control; (2) instances of fraud and noncompliance with provisions of laws or regulations that have a material effect on the audit and any other instances that warrant the attention of those charged with governance; (3) noncompliance with provisions of contracts or grant agreements that has a material effect on the audit; and (4) abuse that has a material effect on the audit.

The American Institute of Certified Public Accountants defines significant deficiencies and material weaknesses in its Codification of Statements on Auditing Standards, section 265, as follows:

.07 For purposes of generally accepted auditing standards, the following terms have the meanings attributed as follows:

Material weakness. 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.

Significant deficiency. 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.

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*

State of Washington Department of Ecology Water Pollution Control State Revolving Fund July 1, 2012 through June 30, 2013

Maia Bellon, Director
Department of Ecology
Olympia, Washington

We have audited, 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, the financial statements of the Department of Ecology's Water Pollution Control State Revolving Fund, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements, and have issued our report thereon dated May 29, 2014. As discussed in Note 1 to the financial statements, during the year ended June 30, 2013, the Agency implemented Governmental Accounting Standards Board Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audits of the SRF's financial statements, we considered the Department'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 Department's internal control. Accordingly, we do not express an opinion on the effectiveness of the Department'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 Fund'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 and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Audit Findings and Responses as Finding 1, that we consider to be significant deficiencies.

COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the SRF's financial statements are free from material misstatement, we performed tests of the SRF's 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.

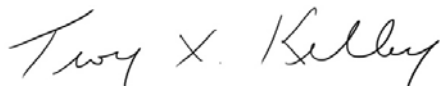
The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

DEPARTMENT'S RESPONSE TO FINDINGS

The Department's response to the findings identified in our audit is described in the accompanying Schedule of Audit Findings and Responses. The Department's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on the response.

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 Department'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 Department's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.



TROY KELLEY
STATE AUDITOR

May 29, 2014

Independent Auditor's Report on Financial Statements

Department of Ecology Water Pollution Control State Revolving Fund July 1, 2012 through June 30, 2013

Maia Bellon, Director
Department of Ecology
Olympia, Washington

REPORT ON THE FINANCIAL STATEMENTS

We have audited the accompanying financial statements of the Department of Ecology's Water Pollution Control State Revolving Fund, as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed on page 9.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. 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. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State Revolving Fund of the Department of Ecology's Water Quality Program as of June 30, 2013, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Matters of Emphasis

As discussed in Note 1, the financial statements present only the Water Pollution Control State Revolving Fund and do not purport to, and do not, present fairly the financial position of the Washington State Department of Ecology as of June 30, 2013, the changes in its financial position, or, where applicable, its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As further discussed in Note 1 to the financial statements, in 2013, the Department adopted new accounting guidance, Governmental Accounting Standards Board Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position*. Our opinion is not modified with respect to this matter.

The financial statements include partial prior year comparative information. Such information does not include all of the information required for a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Fund's financial statements for the year ended June 30, 2012, from which such partial information was derived.

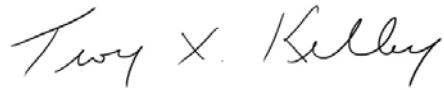
Other Matters

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the State Revolving Fund's basic financial statements as a whole. The management discussion and analysis on pages 10 through 11 is not a required part of the basic financial statements but is supplementary information presented for purposes of additional analysis. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

OTHER REPORTING REQUIRED BY GOVERNMENT AUDITING STANDARDS

In accordance with *Government Auditing Standards*, we have also issued our report dated May 29, 2014, on our consideration of the Department'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 Department's internal control over financial reporting and compliance.

A handwritten signature in cursive script that reads "Troy X. Kelley".

TROY KELLEY
STATE AUDITOR

May 29, 2014

Financial Section

Department of Ecology Water Pollution Control State Revolving Fund July 1, 2012 through June 30, 2013

SUPPLEMENTARY INFORMATION

Management's Discussion and Analysis – 2013

BASIC FINANCIAL STATEMENTS

Comparative Statement of Net Position/Balance Sheet – 2013 and 2012
Comparative Statement of Revenues, Expenses and Changes in Net Position/
Equity – 2013 and 2012
Comparative Statement of Cash Flows – 2013 and 2012
Notes to Financial Statements – 2013

Management Discussion and Analysis

This Management Discussion and Analysis (MD&A) introduces the annual financial statements of the Washington State Water Pollution Control Revolving Fund (SRF) for the year ended June 30, 2013, and supplements these financial statements. The Washington State Department of Ecology (Ecology) SRF loan program is responsible for the content of these financial statements. The MD&A provides readers with a summary of the issues and information Ecology management hopes is useful to the reader.

The Water Pollution Control Revolving Fund Program

The SRF Account was established to provide financial assistance in the form of low-interest loans to local governments and tribes for high priority water quality projects. Ecology receives an annual grant from the U.S. Environmental Protection Agency (EPA). The State Fiscal Year 2013 grant award was \$24,578,000. Ecology matches 20 percent of the grant award with state funds, or \$4,915,600 for 2013. The funding levels for the SRF Program for each fiscal year are based on federal appropriations, state legislative appropriations, repayments from past loans, interest on investments and de-obligated funds. The funding made available for projects in State fiscal year 2013 was \$75,387,311 as published in Ecology's State fiscal year 2013 Intended Use Plan. SRF loan interest rates are between zero and 2.7 percent.

Net position of the SRF

The Washington State SRF program has no capital assets and no related debt. The total amount of reported net position as of June 30, 2013, is \$802,478,498.

Income for fiscal year 2013

Net operating income of the SRF for fiscal year 2013 was \$10,216,709. Operating income or loss includes those amounts earned by the ordinary activities of the program, less the related expenses. Ordinary activities of the program include interest earned on loans and interest earned on balances held with the State Treasurer's Office. Related expenses include salaries and benefits, supplies, travel, indirect costs, and equipment. Net operating income for fiscal year 2012 was \$9,236,687.

Net operating income increases the amount of net position in the program. Other increases to net position include amounts actually received from the EPA capitalization grant and amounts contributed as grant match by the state of Washington. In 2013 the amount of federal funds earned was \$49,824,420 and the amount of state matching funds received during the year was \$7,750,000.

Changes in cash position

During fiscal year 2013 the SRF cash increased by \$36,353,323, as can be seen on the Statement of Net Position. Total loan repayments, including principal and interest received from borrowers was \$52,768,761. Interest credited to the SRF account from the State Treasurer's Office totaled \$304,739. Administrative expenses paid to employees, vendors, and for indirect costs totaled \$1,251,788. Cash received from EPA capitalization grant funds totaled \$49,770,341, and matching funds provided by the state of Washington totaled \$10,905,376. While cash increased from fiscal year 2012 to 2013, Ecology would like to see cash continue to decrease as we award more loans for priority water quality projects throughout the state in 2013.

State matching funds

For State Fiscal Year 2013, State matching funds came from the Public Works Assistance Account. Revenue from this account is derived from a combination of taxes and transfers.

Recovery Act Clean Water State Revolving Fund

During fiscal year 2009, Ecology was appropriated funds under the American Recovery and Reinvestment Act of 2009 (Recovery Act). Enacted on February 17, 2009, due to a national economic crisis, the Recovery Act was intended to stabilize the economy through job creation, provide investments needed to increase economic efficiency by spurring technological advances in science and health, and invest in infrastructure to provide long-term economic benefits.

The Environmental Protection Agency (EPA) awarded a capitalization grant from the Recovery Act for federal fiscal year (FFY) 2009, totaling \$68,151,900. Of this amount, \$65,425,824 was available for projects and \$2,726,076 was available to administer the program. Recovery Act projects are nearing completion. As of July 31, 2013, 98 percent of the project funds have been disbursed.

Conclusion

This MD&A is intended to provide a summary of the financial condition of the SRF loan program and should be read in conjunction with the remainder of this report. The financial statements, footnotes, and supplemental information contained in this annual report provide a detailed analysis of the program's financial position and results of operations.

STATE OF WASHINGTON
WATER POLLUTION CONTROL REVOLVING ACCOUNT
EXHIBIT 3: Comparative Statement of Net Position
June 30, 2013

	2013	2012
Assets:		
Current assets:		
Cash and cash equivalents	\$136,096,750	\$99,743,427
Receivables:		
Due from federal government	57,325	99,539
Interest on SRF loans	2,032,101	2,012,951
Other Receivables	0	0
Due from other funds	117,533	3,193,346
Total receivables	2,206,959	5,305,837
Collateral Held/Security Lending Agreements	5,808,697	0
Current maturities of SRF loans	41,399,726	37,801,183
Total current assets	185,512,132	142,850,447
Loans receivable, net of current maturities	625,456,541	598,008,111
Total assets	810,968,673	740,858,558
Liabilities and Net Position:		
Current liabilities:		
Due to Federal Government	0	0
Accounts payable and accrued expenses	2,627,007	81,407
Due to other funds	32,842	79,074
Obligation Under Security Lending Agreement	5,808,697	0
Unearned Revenue	16,269	0
Construction costs payable	5,359	962,996
Total current liabilities	8,490,174	1,123,476
Net Position:		
Restricted Net Position	802,478,499	739,735,081
Total Net Position	802,478,499	739,735,081
Total Liabilities and Net Position	\$810,968,673	\$740,858,557

The accompanying notes are an integral part of the financial statements

STATE OF WASHINGTON
WATER POLLUTION CONTROL REVOLVING ACCOUNT
EXHIBIT 4: Comparative Statement of Revenues,
Expenses and Changes in Net Position
June 30, 2013

	2013	2012
Operating Revenues:		
Interest income on SRF loans	\$11,421,732	\$10,834,217
Operating Expenses:		
Salaries and benefits	850,947	1,096,956
Supplies	33,050	27,852
Travel	18,257	14,571
Indirect costs	301,482	411,766
Contracts	0	45,985
Equipment	1,287	399
Total operating expenses	1,205,023	1,597,529
Operating income (loss)	10,216,709	9,236,687
Nonoperating Revenue (Expenses)		
Transfer In	0	0
Interest on investments	323,281	518,470
Funds received from EPA	49,824,420	32,155,161
Funds received from State of Washington	7,750,000	7,750,000
Immaterial Adjustments to Prior Period	0	0
Loan Principal Forgiven	(5,370,992)	(10,859,519)
Total nonoperating revenue (expenses)	52,526,709	29,564,111
Change in Net Position	62,743,418	38,800,798
Net Position, beginning of year 07/01/2012	739,735,081	700,934,282
Net Position, end of year 06/30/2013	\$802,478,499	\$739,735,081

The accompanying notes are an integral part of the financial statements

STATE OF WASHINGTON
WATER POLLUTION CONTROL REVOLVING ACCOUNT
EXHIBIT 5: Comparative Statement of Cash Flows
June 30, 2013

	Actual 2013	Actual 2012
Cash Flows from Operating Activities:		
Receipts from customers	\$12,079,123	\$8,883,679
Payments to employees and suppliers	(1,251,788)	(1,606,373)
Forgivable Principal Loans Disbursements	(5,365,633)	(10,859,519)
Loans Disbursements	(70,778,473)	(46,430,275)
Repayments on loans	40,689,638	46,159,763
Net cash provided (used) by operating activities	(24,627,133)	(3,852,726)
Cash Flows from Non-capital Financing Activities:		
Funds received from EPA	49,770,341	31,840,269
Transfers from other State funds	10,905,376	4,980,084
Net cash provided (used) by non-capital financing activities	60,675,717	36,820,353
Cash Flows from Investing Activities:		
Receipts from interest on investments	304,739	536,820
Net cash provided (used) by investing activities	304,739	536,820
Net cash provided (used)	36,353,323	33,504,447
Cash and cash equivalents, beginning of year	99,743,427	66,238,980
Cash and cash equivalents, end of year	136,096,750	99,743,427
Excess of revenue over expenses (Net Income)	10,216,709	9,236,687
(Increase) decrease in interest on SRF loans	45,765	235,048
(Increase) decrease in current maturities of SRF loans	611,626	(2,185,586)
(Increase) decrease in loans receivable (net)	40,689,638	46,159,763
(Decrease) increase in payables	(70,825,238)	(46,439,119)
(Decrease) increase in forgivable principal loan payable	(5,365,633)	(10,859,519)
Net cash provided (used) by operating activities	(\$24,627,133)	(\$3,852,726)

The accompanying notes are an integral part of the financial statements

The accompanying notes are an integral part of the financial statements

1. Summary of Significant Accounting Policies

Reporting Entity

Washington's Water Pollution Control Revolving Account (The Account) was established pursuant to Title VI of the Federal Water Quality Act of 1987 (the Act) and RCW 90.50A.020. The Act established the State Revolving Fund (SRF) program to replace the construction grants program. The Washington State Department of Ecology (ECY) has exclusive responsibility for management of the SRF, per the Operating Agreement between the U.S. Environmental Protection Agency, Region 10, and the Washington State Department of Ecology. This annual report and the accompanying financial statements are for the SRF and the Account, neither of which are legally separate entities.

Operation of the SRF and the Account

The SRF provides loans at reduced interest rates to finance qualified projects for the construction of publicly owned water pollution control facilities, non-point source pollution control projects, and the development and implementation of estuary conservation and management plans. Loans made by the Account must be repaid within 20 years, and all repayments, including interest and principal, must be credited to the Account.

States are required to provide an additional 20 percent of the Federal capitalization grant amount as matching funds in order to receive the grant from EPA. The State has been awarded \$630,154,697 in capitalization grants from 1989 through June 30, 2013. The State match share for that awarded amount is \$112,400,559. For the period of this report, State match is transferred to the Account from the Public Works Assistance Account (Account No. 058).

The Account is administered by the ECY through the Water Quality Program (the Program). The Program's primary responsibilities for the SRF includes obtaining capitalization grants from EPA, soliciting potential interested parties, negotiating loan agreements with local communities, reviewing and approving payment requests from loan recipients, managing the loan repayments, and conducting inspection and engineering reviews to ensure compliance with all applicable laws, regulations, and program requirements.

The Account does not have any full-time employees. ECY employees charge the Account for actual time worked on SRF activities. The charges include the salaries and benefits of the employees as well as indirect costs allocated to the Account based on direct salary and benefit costs. Employees charging time to the Account are covered by the benefits available to Washington State Employees.

Basis of Accounting

The financial statements for the Account are presented as an enterprise fund and are reported using the economic resources measurement focus and the accrual basis of accounting, whereby revenues are recorded as earned and expenses are recorded when the liability is incurred. The Account is included in the state of Washington's general purpose financial statements as a special revenue account, which uses the modified accrual basis of accounting. Due to differences in reporting methods, there may be differences between the amounts reported in these financial statements and the general purpose financial statements.

New Accounting Standards – In June 2011, the GASB issued Statement of Governmental Accounting Standards No. 63 *“Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.”* This statement identifies and defines deferred outflow of resources, deferred inflow of resources and net position. The Statement also standardizes the presentation of the statements involving the deferred inflows and outflows of resources and net position. The requirements of this Statement are effective for financial statements for periods beginning after December 15, 2011. GASB 63 has been adopted within this report. For the period ending June 30, 2013, the Account did not have any Deferred Outflows or Inflows of resources to present.

Cash and Cash Equivalents

All monies of the Account are deposited with the State Treasurer’s Office and are considered cash. According to State law, the Treasurer is responsible for maintaining the cash balances and investing excess cash of the Account. Consequently, Ecology staff that provide management of the Account do not have control over the investment of the excess cash. The statement of cash flows considers all funds deposited with the Treasurer to be cash or cash equivalents, regardless of actual maturities of the underlying investments.

Loans Receivable

ECY operates the Account as a direct loan program which makes loans to communities through funding by the Federal capitalization grant for 83.3 percent of the loan amount, and funding by State matching for 16.7 percent of the loan amount. Loan funds are disbursed to local entities after they expend funds for the purposes of the loan and then request reimbursement from the Account. Interest is calculated from the date the state warrant is mailed or the Electronic Fund Transfer settlement date. After the final disbursement, the loan amount and repayment schedule are adjusted for actual funds disbursed and interest accrued during the project period. No provision for uncollectible accounts has been made as management believes that all loans will be repaid according to the loan terms.

Forgivable Principal

In SFY12, the federal Appropriations Act of 2011 was passed by Congress. This Act authorized some of the same requirements that were introduced in the American Recovery and Reinvestment Act of 2010. One of these requirements is forgivable principal hardship loans. The maximum forgivable principal loan amount for each hardship recipient is \$5 million. ECY awarded \$1,455,012 in forgivable principal in SFY2013.

Funds from EPA

In accordance with generally accepted accounting principles (GAAP), funds received from EPA and Washington State for the capitalization of the Account are recorded as funds from EPA and the state of Washington, as discussed in Note 4.

2. Deposits and Investments

All monies of the Account are deposited with the State Treasurer’s Office as part of the State’s Treasury/Trust Portfolio, and are considered cash. The Treasurer is responsible for maintaining and investing the pooled cash balances in accordance with State laws. The Treasurer is required to maintain a mix of investment portfolios in order to allow funds to be withdrawn at any time to meet normal operating needs without prior notice or penalty. The Account’s proportionate share of the investment income, based on the average daily balance for the period, is credited to the

Account monthly. The Treasurer charges the Account one-half of one percent of the average daily balance for administration costs. As of June 30, 2013, total Treasurer's invested balance of the Treasury/Trust Fund Portfolio was \$4.75 billion. Details of the investments can be obtained from the State Treasurer's Office.

All cash and investments are stated at cost, which approximates fair market value.

	Carrying Amount	Market Value
Treasury/Trust Portfolio June 30, 2013	<u>\$136,096,750</u>	<u>\$136,096,750</u>

3. Loans Receivable

The Account makes loans to qualified entities for projects that meet the eligibility requirements of the Clean Water Act. Loans are financed by capitalization grants, state matches, and revolving funds. Interest rates for SFY 2013 were established at 1.4 percent for up to a five year-term and 2.7 percent for loans with more than a five-year term, but no more than 20 years. The Account also makes hardship loans with a variable interest rate, as low as zero, to communities that can demonstrate financial hardship on residential ratepayers in the form of sewer user fees. Loan repayments are required to start one year after initiation of operations or project completion, whichever occurs first. Details of loans receivable as of June 30, 2013, are summarized below:

Loans by Category:

Loans receivable by project status at June 30, 2013 are as follows:

	Loan Authorized	Loan Disbursed	Loan Repaid	Remaining Commitment	Receivables Balance
Completed Projects	\$626,274,528	\$626,274,528	\$43,839,171	\$0	\$582,435,357
Projects in Progress	207,446,210	84,420,909	0	123,025,301	84,420,909
Total					\$666,856,266
Payment requests in progress (Received as of June 30, 2013, but not yet paid)					0
Less Amount Due in one year					(41,399,725)
Loans receivable, June 30, 2013 (Net of current maturities)					\$625,456,541

Loans mature at various intervals. The scheduled minimum repayments on completely disbursed loans in subsequent years are as follows:

Year ending June 30:	<u>Amount</u>
2014	\$49,669,124
2015	49,556,940
2016	49,137,054
2017	48,296,441
2018	47,908,874
Thereafter	386,792,462
	<u>\$631,360,895</u>

Loans to Major Local Entities:

As of June 30, 2013, the Account made loans to the following major local entities. The aggregate outstanding balance for each of these entities exceeds \$5 million. The outstanding balances of these loans represent approximately 84 percent of the total loans receivable:

(Figures are in Thousands)

<u>Entity</u>	<u>Authorized Loan Amount</u>	<u>Project Period Interest</u>	<u>Loan Amount At Completion</u>	<u>Outstanding Balance</u>
Alderwood Water & Wastewater Dist	\$ 9,016	\$ 293	\$ 9,309	\$ 8,701
City of Airway Heights	10,895	649	11,544	11,127
City of Arlington	14,558	405	14,963	14,242
City of Bremerton	9,921	155	10,017	6,611
City of Camas	14,364	816	15,180	9,644
City of Centralia	38,705	120	38,094	22,842
City of Chehalis	35,343	44	35,388	25,124
City of Cheney	12,929	1	12,930	9,939
City of Longview	10,767	333	11,099	10,754
City of Mt. Vernon	18,785	764	19,549	15,428
City of Pasco	22,726	2,284	25,011	9,941
City of Sequim	10,864	136	11,000	6,441
City of Stanwood	9,306	0	9,306	5,383
City of Sunnyside	12,377	0	12,377	8,886
City of Tacoma	73,701	1,952	75,652	61,013
City of Toppenish	11,962	0	11,962	9,352
City of Walla Walla	13,780	831	14,610	6,302
City of Wenatchee	7,195	197	7,392	5,356
City of Winlock	6,635	4	6,638	5,258
King Co. Dept. Nat. Resources	168,116	11,739	169,992	87,846
King Co. Wastewtr. Treat. Div.	26,769	103	26,872	17,286
King County	21,046	193	21,239	11,001
Kitsap County Public Works	10,173	178	10,351	6,682
Lake Stevens Sewer District	45,202	4,230	49,432	48,023
Lott Wastewater Alliance	108,265	6,401	105,620	56,015
Mason County	21,313	444	21,742	11,779
Seattle Public Utilities	11,815	310	11,583	10,451
Spokane County	19,140	94	19,234	12,260
Spokane County Conservation District	<u>14,176</u>	<u>377</u>	<u>14,553</u>	<u>9,523</u>
Total	<u>\$789,844</u>	<u>\$33,053</u>	<u>\$802,639</u>	<u>\$523,210</u>

The loan amount at completion may not agree with the authorized loan amount plus capitalized project period interest. Communities may elect to pay capitalized project period interest

separately or add the amount to the final loan amount. Further, the authorized loan amount is based on estimates, and final project costs may be different than estimated.

4. Funds from EPA and the State of Washington

(Figures are in Thousands)

The Account is funded by grants from EPA authorized by the Clean Water Act and by matching funds from the State. All funds drawn are recorded as non-operating revenue from the EPA and Washington State. Since 1989, EPA has awarded a total of \$630,155 in grants to the State, of which \$582,174 has been drawn for loans and administrative expenses. The State has provided a total of \$103,024 in matching funds for that total drawn amount. The following summarizes the grants awarded, amounts drawn on each grant as of the balance sheet date, and balances available for future loans:

Grant Year	Grant Amount	Draws through SFY 2012	2013 Draws	Draws through SFY 2013	Available SFY 2013
1989-1991	\$70,278	\$70,278	\$0	\$70,278	\$0
1992	33,789	33,789	0	33,789	0
1993	33,425	33,425	0	33,425	0
1994	20,740	20,740	0	20,740	0
1995	21,420	21,420	0	21,420	0
1996	22,509	22,509	0	22,509	0
1997	23,415	23,415	0	23,415	0
1998	23,417	23,417	0	23,417	0
1999	46,759	46,759	0	46,759	0
2001	23,132	23,132	0	23,132	0
2002	23,184	23,184	0	23,184	0
2003	23,033	23,033	0	23,033	0
2004	23,047	23,047	0	23,047	0
2005	18,739	18,739	0	18,739	0
2006	26,347	26,347	0	26,347	0
2007	19,410	19,410	0	19,410	0
2008	11,834	11,834	0	11,834	0
2008 (ARRA)	68,152	65,515	1,541	67,056	1,096
2009	11,834	1,027	10,807	11,834	0
2010	35,433	1,181	34,252	35,433	0
2011	25,680	148	3,225	3,373	22,307
2012	24,578	0	0	0	24,578
	\$630,155	\$532,349	\$49,825	\$582,174	\$47,981

As of SFY 2013, State matching contributions were:

	<u>SFY 2012</u>	<u>2013 Contribution</u>	<u>SFY 2013</u>
Washington State Matching Contributions	<u>\$93,370</u>	<u>\$9,654</u>	<u>\$103,024</u>

5. Contingencies and Subsequent Events

Contingencies

The Account is exposed to various risks of loss, related to torts, thefts of assets, errors or omissions, injuries to state employees while performing Account business, or acts of God.

The Account maintains insurance for all risks of loss which is included in the indirect costs allocated to the Account. There have not been any claims against the Account since its inception in 1989 and no contingencies came to our attention during our audit which requires disclosure or accrual under Statement of Financial Accounting Standards No. 5.

Subsequent Events

No events occurring subsequent to the balance sheet date came to our attention which requires adjustment to, or disclosure in, the financial statements.



ABOUT THE STATE AUDITOR'S OFFICE

The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

We work with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

The State Auditor's Office employees are located around the state to deliver services effectively and efficiently.

Our audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. In addition, we conduct performance audits of state agencies and local governments and fraud, whistleblower and citizen hotline investigations.

The results of our work are widely distributed through a variety of reports, which are available on our Web site and through our free, electronic subscription service.

We take our role as partners in accountability seriously. We provide training and technical assistance to governments and have an extensive quality assurance program.

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