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CLEAN WATER ACT

Use of State Revolving Funds Varies

Statement for the Record by
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Mr. Chairman and Members of the Subcommittee:

To assist the Subcommittee's consideration of the Environmental Protection Agency's (EPA) fiscal year 1997 budget request, we are pleased to submit this statement on the preliminary results of our review, being performed at your request, of the State Water Pollution Control Revolving Fund (SRF) Program. The program provides federal financial assistance primarily to help communities build wastewater treatment facilities and, thereby, meet the requirements of the Federal Water Pollution Control Act, as amended, known as the Clean Water Act. We expect to report fully this summer on the results of our work, including a questionnaire we sent to nine states.

Specifically, this statement provides information on: (1) how much of their available funds have the states lent for wastewater treatment facilities and related purposes and (2) what impediments are the states encountering in making these loans.

In summary, the states had made loans totalling $14.6 billion, or 77 percent of the available funds, as of June 30, 1995, according to a survey by the Ohio State Water Development Authority,[1] the only known source of data for all states. The proportion of funds lent varied widely among the states. Also, we found that the states encountered various impediments in lending their SRF funds. These include (1) some states' lack of experience in managing lending programs, (2) financial factors, such as the inability of small communities to afford SRF loans and the ability of certain large communities to borrow at lower rates from the bond market, and (3) other, state-specific factors.

Background

The Congress established the Construction Grants Program in 1972 to provide non-repayable grants (funded primarily by the federal government, with state assistance) to help local governments pay for the construction of wastewater treatment facilities. In the 1987 amendments to the Clean Water Act, the Congress phased out the Construction Grants Program and authorized the creation of state revolving funds, which provide repayable loans to local governments. All 50 states and Puerto Rico have established SRFS.

[1]Between 1992 and 1995, the Ohio authority annually surveyed all 50 states and Puerto Rico on certain aspects of the SRF program.

Under the SRF program, the federal government provides grants to the states as "seed money" to capitalize their revolving loan funds. The states are required to match the federal grants, at a rate of one state dollar for every five federal dollars. The states use their revolving funds to make loans to local governments and, as loans are repaid, the fund is replenished. The states may use SRF funds for estuary protection and nonpoint-source pollution control, as well as wastewater treatment facilities.

As of June 30, 1995, according to the Ohio authority, the states collectively had received $18.9 billion in their SRFs, comprised of several sources. Over one-half of this amount, about $10 billion, came from new federal grants and about $1 billion more from unused construction grants that the states transferred to their revolving funds. Other substantial sources included funds borrowed by the states ($5.4 billion)[2] and state matching and other funds ($2.4 billion).

The transfer of federal funds to SRFs begins when the Congress appropriates funds to EPA. EPA then allots funds to individual states generally according to percentages specified in the Clean Water Act. To receive its allotment, a state must provide EPA—within 2 years—with a list of projects that it expects to fund. A state generally has up to 2 years to receive payment of its allotment and, after receiving its payment, has up to 1 year to make binding commitments to fund specific projects. Next, a binding commitment is typically converted into a loan agreement.[3] As work on a project is completed and contractors submit invoices for payments, EPA generally authorizes payments to the contractors. The law requires that SRF funds be used in an "expeditious and timely manner," but neither the law nor EPA's regulations specifically define these terms.

Lending Rates Vary Widely Among the States

Overall, the states had lent $14.6 billion, or 77 percent, of the $18.9 billion cumulatively available to them, as of June 30, 1995, according to the only available data we were able to identify that cover all states' activities. These data were collected by the Ohio authority.[4]

[2]A state is authorized to use money from its SRF to secure a bond issue (debt). The state then uses the proceeds from the sale of bonds to augment its SRF. This is called leveraging. According to the Ohio data, 21 states have leveraged their SRFs.

[3]In some states, according to an EPA official, a binding commitment is equivalent to a loan agreement.

[4]The Ohio authority's 1995 report acknowledges that certain state data are inconsistent. Nevertheless, we believe the data can be useful in identifying program trends.

Although the states collectively had lent 77 percent of their available funds, lending rates varied considerably from state to state. For example, 8 states had lent more than 90 percent of their available funds. Conversely, 11 states had lent less than 60 percent, including 3 states that had lent less than 40 percent.

We relied on the Ohio authority data because EPA does not compile nationwide data on SRF lending. EPA officials told us that they are developing their own information system. Called the SRF Information Management System, it is expected to begin operating later this year and to include nationwide information on the states' lending of SRF funds. The officials said that such data may help identify the states that may be having difficulty using SRF funds.

Managerial, Financial, and Other Factors Constrain States' Lending of SRF Funds

Through our discussions and visits with EPA and state officials, we identified a number of impediments that have constrained states' lending of SRF funds. These include managerial, financial, and other, state-specific factors.

The states' experience in managing loan programs has affected how quickly they lent SRF funds, especially in the early years of the SRF program. However, this factor should become less important as the states gain experience in managing their revolving funds. For example, in Texas, which had a state fund for financing wastewater infrastructure before the SRF program was authorized, officials told us that their state program experience allowed them to operate the SRF efficiently. This is reflected in Texas' lending rate—81 percent as of August 1995[5], a relatively high rate.

In contrast, Louisiana, with no comparable experience prior to the SRF program, had more difficulty at the beginning. In the first 6 years of the SRF program, Louisiana made loans totalling $49 million, but in the seventh year alone it made loans totalling $38 million. Thus, Louisiana's lending rate rose from 48 percent as of June 1994 to 65 percent as of June 1995.[6]

Financial factors can affect whether both small and large communities apply for SRF loans. For example, state officials in Louisiana and

[5]Although the lending rate for Texas was 64 percent according to the Ohio data, on the basis of our discussions with Texas officials and review of documents, we estimate that the lending rate was 81 percent. Texas' fiscal year is September 1 to August 31.

[6]We derived these estimates on the basis of discussions with state officials and review of documents. These rates are within 2 percentage points of the data reported by the Ohio authority.

Pennsylvania said that many small communities cannot afford to repay a loan because they do not have enough ratepayers among whom to spread a project's costs and that such communities, therefore, often do not apply for loans. At the other end of the population spectrum, state officials told us that large communities with good credit ratings may be able to borrow money via the bond market at rates that are more favorable, or with fewer restrictions, than those offered by their SRF.

Also, Maryland and Pennsylvania officials said that some communities are reluctant to apply for a SRF loan because they hoped to obtain a non-repayable federal grant or have withdrawn their applications for SRF loans after receiving such a grant. The sources for such grants include the Department of Housing and Urban Development's Community Development Block Grant Program and the Department of Agriculture's Rural Development Administration grants.[7]

Finally, there are other, state-specific factors that affect the states' use of SRF funds. For example, in Arizona all public projects, including those financed with SRF loans, must be approved by the voters before loans can be awarded. According to Arizona officials, voters did not approve any projects that were ready to proceed with SRF financing last year, and the state postponed loan closings until at least August 1995.

[7]As we reported last year, 8 federal agencies administer 17 different programs that are designed specifically for, or that may be used by, rural areas for constructing, expanding, or repairing water and wastewater facilities. See Rural Development: Patchwork of Federal Water and Sewer Programs Is Difficult to Use (GAO/RCED-95-160BR, Apr. 13, 1995).

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