



Certified Public Accountants and Consultants

**State of Delaware
Delaware Water Pollution Control
Revolving Loan Fund
Dover, Delaware**

**Financial Statements
Years Ended June 30, 2016 and 2015**

Report Issued: February 8, 2017

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Independent Auditor's Report

To the Management
Delaware Water Pollution Control
Revolving Loan Fund
State of Delaware

Report on the Financial Statements

We have audited the accompanying financial statements of the Delaware Water Pollution Control Revolving Loan Fund (the Fund) of the State of Delaware, as of and for the years ended June 30, 2016, and 2015, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Fund as of June 30, 2016 and 2015, and the respective 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.

Emphasis of Matter

As discussed in Note 2, the financial statements present only the State of Delaware Water Pollution Control Revolving Loan Fund and do not purport to, and do not, present fairly the financial position of the State of Delaware as of June 30, 2016 and 2015, and the changes in its financial position, or its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated January 19, 2017 on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Fund's internal control over financial reporting and compliance.

January 19, 2017

Gunnip & Company LLP

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Management's Discussion and Analysis
June 30, 2016

As management of the Delaware Water Pollution Control Revolving Loan Fund (the Fund), we offer readers of the Fund's financial statements this narrative overview and analysis of the financial activities of the Fund for the fiscal year ended June 30, 2016 (fiscal year 2016).

This section of the Fund's annual financial report presents management's discussion and analysis of the financial performance during the fiscal year. Please read it in conjunction with the Fund's financial statements, which follow this section.

Overview of the Financial Statements

This discussion and analysis is an introduction to the Fund's basic financial statements. The Fund's basic financial statements are comprised of two components: Fund financial statements and notes to the financial statements.

Financial Highlights

In fiscal year 2016, the Delaware Department of Natural Resources and Environmental Control (DNREC) was awarded a Federal Capitalization Grant for \$6,817,000 from the U.S. Environmental Protection Agency (EPA). As of June 30, 2016, DNREC has received Federal Capitalization Grants in an aggregate amount of \$226,174,510 since the inception of the Fund. As of June 30, 2016, the State of Delaware has provided State match funds of \$41,387,084 since the inception of the Fund. The combined total capitalization amount at June 30, 2016 was \$267,561,594 since the inception of the Fund.

The Fund realized operating income of \$763,507 in fiscal year 2016, which represents an increase of \$19,559, from the fiscal year ended June 30, 2015 (fiscal year 2015). Contributions from the federal and State governments totaled \$15,401,280 in fiscal year 2016, an 82% increase from fiscal year 2015.

Operating revenues for fiscal year 2016 (including interest income on loans) decreased \$75,927 or 2% from the previous year. Operating revenues for fiscal year 2015 (including interest income on loans) increased \$639,820 or 20% from the previous fiscal year.

Loans disbursements made totaled \$13,807,706 during the fiscal year 2016, which represents an increase of \$5,271,784 or 62% from fiscal year 2015. The increase in loan disbursements from fiscal year 2015 to fiscal year 2016 is primarily due to two loan disbursements. Loans collections totaled \$11,086,008 during fiscal year 2016 which represents a decrease of \$847,309 or 7% from fiscal year 2015.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Management's Discussion and Analysis - Continued
June 30, 2016

Statement of Net Position

The following schedule summarizes the statements of net position (thousands of dollars) of the Fund as of June 30, 2016, 2015 and 2014:

	June 30,		
	2016	2015	2014
Current assets			
Pooled cash and investments	\$108,516	\$ 98,045	\$ 85,068
Grants receivable	2,517	54	170
Administrative fees receivable	274	293	256
Interfund receivable	562	588	649
Due from Drinking Water	166	-	-
Interest receivable	332	352	264
Loans receivable, current	9,942	10,959	12,122
Total current assets	122,309	110,291	98,529
Noncurrent assets			
Loans receivable, less current portion	163,027	159,035	162,611
Total assets	<u>\$285,336</u>	<u>\$269,326</u>	<u>\$261,140</u>
Current liabilities			
Vouchers payable	\$ 1,310	\$ 109	\$ 219
Unearned state match	788	1,911	1,953
Interfund payable	562	588	649
Total liabilities	2,660	2,608	2,821
Net position - unrestricted	282,676	266,718	258,319
Total liabilities and net assets	<u>\$285,336</u>	<u>\$269,326</u>	<u>\$261,140</u>

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Management's Discussion and Analysis - Continued
June 30, 2016

Statement of Net Position - Continued

The combined total net position of the Fund for the fiscal year ended June 30, 2016 increased by \$15,958,484 from fiscal year 2015, which increased by \$8,398,734 from the fiscal year ended June 30, 2014 (fiscal year 2014).

Pooled cash and investments increased \$10,471,002 or 11% to \$108,516,132 during fiscal year 2016, as a function of loan collections and federal reimbursements.

Pooled cash and investments increased \$12,976,818 or 15% to \$98,045,130 during fiscal year 2015, as a function of loan collections and federal reimbursements, as well as a decrease in loan disbursements compared to the prior year.

Unearned income from the State match decreased \$1,123,321 or 59% during fiscal year 2016, as the Fund recognized its match to fund operating expense and loan disbursements to borrowers.

Unearned income from the State match decreased \$41,850 or 2% during fiscal year 2016, as the Fund recognized its match to fund operating expense and loan disbursements to borrowers.

Statement of Revenues, Expenses and Changes in Net Position

The following schedule summarizes the statements of revenues, expenses and changes in net position (thousands of dollars) for fiscal years 2016, 2015 and 2014:

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Management's Discussion and Analysis - Continued
June 30, 2016

Statement of Revenues, Expenses and Changes in Net Position - Continued

		June 30,	
	2016	2015	2014
Operating revenues			
Interest income on loans	\$ 1,926	\$ 1,935	\$ 1,422
Administrative fee revenue	1,823	1,890	1,763
Application fees	1	1	1
Other income	1	1	1
Total operating revenues	<u>3,751</u>	<u>3,827</u>	<u>3,187</u>
Operating expenses			
Reimbursable expenditures under operating grants:			
Personnel costs	1,239	1,293	1,291
Travel	10	8	10
Contractual services	344	309	301
Supplies	10	13	12
Other expenses	45	13	289
Grants made	<u>1,339</u>	<u>1,447</u>	<u>1,296</u>
Total operating expenses	<u>2,987</u>	<u>3,083</u>	<u>3,199</u>
Operating income (loss)	<u>764</u>	<u>744</u>	<u>(12)</u>
Nonoperating revenues (expenses)			
Interest income on deposits	637	378	265
Contributions, EPA	12,834	7,069	26,952
Contributions, State	2,567	1,412	5,392
Loan forgiveness and write-offs	<u>(844)</u>	<u>(1,204)</u>	<u>(165)</u>
Total nonoperating revenues	<u>15,194</u>	<u>7,655</u>	<u>32,444</u>
Change in net position	15,958	8,399	32,432
Net position - beginning	<u>266,718</u>	<u>258,319</u>	<u>225,887</u>
Net position - ending	<u><u>\$282,676</u></u>	<u><u>\$266,718</u></u>	<u><u>\$258,319</u></u>

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Management's Discussion and Analysis - Continued
June 30, 2016

Statement of Revenues, Expenses and Changes in Net Position - Continued

The Fund reported operating revenues of \$3,750,567 during fiscal year 2016, which represents a decrease of \$75,927 or 2% from fiscal year 2015. The Fund reported operating revenues of \$3,826,494 during fiscal year 2015, which represents an increase of \$639,820 or 20% from fiscal year 2014. The decrease in the current fiscal year is primarily a result of decreased interest and administrative fee income, which were monies received as part of loan repayments. Borrowers are required to pay interest and administrative fees on funds disbursed during construction as well as throughout the life of the loan. Due to a decrease in new loans issued in the prior year, income from interest and administrative fees decreased. The Fund reported an overall increase of \$15,958,484 in total net position for fiscal year 2016, and an overall increase of \$8,398,743 in total net position for fiscal year 2015.

Federal grant revenue increased by \$5,765,624 or 82% during fiscal year 2016, while the State match increased by \$1,154,669, or 82%.

Federal grant revenue decreased by \$19,883,400 or 74% during fiscal year 2015, while the State match decreased by \$3,979,477, or 74%.

Total operating expenses decreased \$95,486 or 3% during fiscal 2016, due to an decrease in grants made and personnel expenses paid out of the Nonfederal Administrative Fund. Total operating expenses decreased \$116,683 or 4% during fiscal year 2015, due to a decrease in other expenses paid out of the Federal Administrative Fund.

During fiscal year 2016, the Fund recognized nonoperating expenses \$843,840 for loan forgiveness and write-offs compared to \$1,203,904 in fiscal year 2015.

Requests for Information

This financial report is designed to provide a general overview of the Fund's finances to the users of such data. Requests for additional copies of this report, questions concerning any of the information in this report, and requests for additional financial information should be addressed to:

Terry Deputy
State of Delaware
Department of Natural Resources & Environmental Control
Division of Water Resources
5 E. Reed Street, Suite 200
Dover, Delaware 19901

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Statement of Net Position
June 30, 2016 and 2015

	2016				2015			
	Federal Administrative Fund	Capital Reserve Loan Fund	Nonfederal Administrative Fund	Total	Federal Administrative Fund	Capital Reserve Loan Fund	Nonfederal Administrative Fund	Total
Current assets								
Pooled cash and investments	\$ -	\$ 102,530,704	\$ 5,985,428	\$ 108,516,132	\$ -	\$ 91,287,869	\$ 6,757,261	\$ 98,045,130
Grants receivable	-	2,516,994	-	2,516,994	-	53,894	-	53,894
Administrative fees receivable	-	-	273,603	273,603	-	-	292,708	292,708
Interfund receivable	-	-	562,163	562,163	-	-	588,111	588,111
Due from Drinking Water	-	132,124	33,943	166,067	-	-	-	-
Interest receivable	-	332,100	-	332,100	-	351,570	-	351,570
Loans receivable - current	-	9,942,352	-	9,942,352	-	10,959,431	-	10,959,431
Total current assets	-	115,454,274	6,855,137	122,309,411	-	102,652,764	7,638,080	110,290,844
Noncurrent assets								
Loans receivable, less current portion	-	163,026,899	-	163,026,899	-	159,034,825	-	159,034,825
Total assets	\$ -	\$ 278,481,173	\$ 6,855,137	\$ 285,336,310	\$ -	\$ 261,687,589	\$ 7,638,080	\$ 269,325,669
Current liabilities								
Vouchers payable	\$ -	\$ 1,309,899	\$ -	\$ 1,309,899	\$ -	\$ 108,473	\$ -	\$ 108,473
Unearned state match	-	788,063	-	788,063	-	1,911,384	-	1,911,384
Interfund payable	-	562,163	-	562,163	-	588,111	-	588,111
Total liabilities	-	2,660,125	-	2,660,125	-	2,607,968	-	2,607,968
Net position-unrestricted	-	275,821,048	6,855,137	282,676,185	-	259,079,621	7,638,080	266,717,701
Total liabilities and net position	\$ -	\$ 278,481,173	\$ 6,855,137	\$ 285,336,310	\$ -	\$ 261,687,589	\$ 7,638,080	\$ 269,325,669

See accompanying notes to financial statements.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund
Statement of Revenues, Expenses and Changes in Net Position
Years Ended June 30, 2016 and 2015

	2016				2015			
	Federal Administrative Fund	Capital Reserve Loan Fund	Nonfederal Administrative Fund	Total	Federal Administrative Fund	Capital Reserve Loan Fund	Nonfederal Administrative Fund	Total
Operating revenues								
Interest income on loans	\$ -	\$ 1,925,843	\$ -	\$ 1,925,843	\$ -	\$ 1,934,512	\$ -	\$ 1,934,512
Administrative fee revenue	-	-	1,822,901	1,822,901	-	-	1,890,316	1,890,316
Application fees	-	1,009	-	1,009	-	814	-	814
Other income	-	814	-	814	-	852	-	852
Total operating revenues	-	1,927,666	1,822,901	3,750,567	-	1,936,178	1,890,316	3,826,494
Operating expenses								
Reimbursable expenditures under operating grants:								
Personnel costs	301,056	-	937,946	1,239,002	58,171	-	1,235,190	1,293,361
Travel	-	-	9,843	9,843	-	-	7,782	7,782
Contractual services	480	-	343,285	343,765	28,501	-	280,963	309,464
Supplies and office expenses	-	-	10,343	10,343	-	-	12,540	12,540
Other expenses	40,749	197	4,150	45,096	3,955	433	8,301	12,689
Grants made	-	-	1,339,011	1,339,011	-	-	1,446,710	1,446,710
Total operating expenses	342,285	197	2,644,578	2,987,060	90,627	433	2,991,486	3,082,546
Operating income (loss)	(342,285)	1,927,469	(821,677)	763,507	(90,627)	1,935,745	(1,101,170)	743,948
Nonoperating revenues and expenses								
Interest income on deposits	-	598,803	38,734	637,537	-	347,134	30,569	377,703
Contributions:								
EPA	284,826	12,549,335	-	12,834,161	75,113	6,993,424	-	7,068,537
State	57,459	2,509,660	-	2,567,119	15,514	1,396,936	-	1,412,450
Loan forgiveness and write-offs	-	(843,840)	-	(843,840)	-	(1,203,904)	-	(1,203,904)
Total nonoperating revenues and expenses	342,285	14,813,958	38,734	15,194,977	90,627	7,533,590	30,569	7,654,786
Change in net position	-	16,741,427	(782,943)	15,958,484	-	9,469,335	(1,070,601)	8,398,734
Net position - beginning - unrestricted	-	259,079,621	7,638,080	266,717,701	-	249,610,286	8,708,681	258,318,967
Net position - end - unrestricted	\$ -	\$ 275,821,048	\$ 6,855,137	\$ 282,676,185	\$ -	\$ 259,079,621	\$ 7,638,080	\$ 266,717,701

See accompanying notes to financial statements.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Statement of Cash Flows
Years Ended June 30, 2016 and 2015

	2016	2015
Cash flows from operating activities		
Loan collections	\$ 11,086,008	\$ 11,933,317
Interest received from borrowers	1,945,313	1,847,200
Administrative fee revenue	1,842,006	1,853,172
Application fees and other revenue	1,823	1,666
Loan disbursements	(13,807,706)	(8,535,922)
General expenses paid	(3,005,040)	(3,055,873)
Net cash provided by (used in) operating activities	<u>(1,937,596)</u>	<u>4,043,560</u>
Cash flows from noncapital financing activities		
Grants received from EPA	10,371,061	7,184,955
State portion funded by recipient	1,400,000	1,370,600
Net cash provided by noncapital financing activities	<u>11,771,061</u>	<u>8,555,555</u>
Cash flows from investing activities		
Interest on deposits	<u>637,537</u>	<u>377,703</u>
Net increase in pooled cash and investments	10,471,002	12,976,818
Pooled cash and investments - beginning of year	<u>98,045,130</u>	<u>85,068,312</u>
Pooled cash and investments - end of year	<u><u>\$ 108,516,132</u></u>	<u><u>\$ 98,045,130</u></u>
Reconciliation of net operating income to cash provided by (used in) operating activities:		
Cash flows from operating activities:		
Operating income	\$ 763,507	\$ 743,948
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:		
Administrative fees receivable	19,105	(37,144)
Interest receivable	19,470	(87,312)
Loans receivable	(3,818,835)	3,534,375
Due from Drinking Water	(166,067)	-
Vouchers payable	1,245,224	(110,307)
Net cash provided by (used in) operating activities	<u><u>\$ (1,937,596)</u></u>	<u><u>\$ 4,043,560</u></u>
Schedule of noncash investing activities		
Loan forgiveness and write-offs	<u><u>\$ (843,840)</u></u>	<u><u>\$ (1,203,904)</u></u>

See accompanying notes to financial statements.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements
June 30, 2016 and 2015

Note A - Summary of Significant Accounting Policies

This summary of significant accounting policies of the Delaware Water Pollution Control Revolving Loan Fund (the Fund) is presented to assist in understanding the Fund's financial statements. The financial statements and notes are representations of the Fund's management which is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

1. General Background

The Fund was created by the 1990 session of the Delaware General Assembly and received its first State appropriation on July 1, 1990. The Fund's purpose is to make below-market interest rate loans to local governments, individuals, and other qualifying applicants under the Environmental Protection Agency's (EPA) Capitalization Grants for State Revolving Funds (SRF) federal assistance program. The Fund's enabling legislation empowers the Department of Natural Resources and Environmental Control (DNREC) to administer the Fund.

2. Type of Entity and Division of Funds

The Fund's activities are accounted for as a distinct operating unit and a Proprietary Fund within DNREC's Office of the Secretary. Accordingly, the financial statements of the Fund are intended to present the financial position, results of operations and cash flows of Proprietary Fund types of only that portion of the funds of the State of Delaware (the State) that are attributable to the transactions of the Fund.

The Fund is divided into three sub-funds:

- The Federal Administrative Fund, which accounts for program-related administrative activities;
- The Capital Reserve Loan Fund, which accounts for capital lending and repayment activities; and
- The Nonfederal Administrative Fund, which accounts for monies that the State has been authorized, by the EPA, to allocate from the SRF program for the State's use. The use of these funds are governed by EPA rules and regulations 40 CFR Part 35 Guidance on Fees Charged by State to Recipients of Clean Water State Revolving Fund Program Assistance.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note A - Summary of Significant Accounting Policies - Continued

3. Measurement Focus and Basis of Accounting

The accompanying financial statements of the Fund have been prepared using the economic resources measurement focus and the accrual basis of accounting in conformity with United States generally accepted accounting principles applicable to governmental entities as prescribed by the Governmental Accounting Standards Board (GASB). The Fund's activities are financed and operated as an enterprise fund. When an expense is incurred that can be paid using either restricted or unrestricted resources, it is the Fund's policy to first apply the expense towards restricted resources and then toward unrestricted resources.

The Fund has elected to apply all applicable GASB pronouncements as well as any applicable pronouncements of the Financial Accounting Standards Board (FASB), the Accounting Principles Board or any Accounting Research Bulletins issued on or before November 30, 1989 unless those pronouncements conflict with or contradict GASB pronouncements. The Fund has elected not to follow subsequent private-sector (FASB) guidance.

4. Recognition of Revenues

Federal assistance provided by the Capitalization Grants for the SRF program is earned when qualified expenditures are incurred by the borrowers and the Fund. Matching funds provided by the State are considered earned by the same criteria. Amounts earned in excess of grant monies received from the EPA are recorded as grants receivable. Amounts received from the State in excess of amounts earned are considered deferred grant revenue and recorded as unearned State match.

To permit comparability to grant revenues earned and fiscal budgets, expenditures reimbursable under the Fund's program guidelines are listed separately by object category and subtotaled in the statement of revenues, expenses and changes in net position.

Operating revenues include those that result from the Fund's lending activities. Nonoperating revenues include those from noncapital financing and investing activities.

5. Pooled Cash and Investments

Pooled cash and investments consist of the Fund's allocated share of cash, cash equivalents and investments under the control of the Treasurer of the State of Delaware.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note A - Summary of Significant Accounting Policies - Continued

6. Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Note B - Pooled Cash and Investments

Pooled Cash and Investments

Pooled cash and investments as reported on the statement of net position represent the Fund's allocated share of cash, cash equivalents and investments under the control of the Treasurer of the State of Delaware (Treasurer). All cash is deposited with the Treasurer by State agencies and maintained by the Treasurer in various pooled funds. The Treasurer invests the deposited cash, including cash float in short-term securities and other investments. Interest income is credited to the Fund based on the weighted average rate of return on the State's monies applied to the Fund's average daily cash balance. Pooled investments represent those investments in units of a pool rather than specific securities. As a result, such investments are not categorized by risk because they are not evidenced by securities that exist in a physical or book-entry form. Since the Fund's deposits and investments are part of the State's pooled deposits and investments maintained by the Treasurer, the required disclosures are included within the State of Delaware's financial statements.

The Cash Management Policy Board

The State's policy for the investment of State funds is the responsibility of the Cash Management Policy Board (the Board). The Board, created by State law, establishes policies for and the terms, conditions, and other matters relating to the investment of all money belonging to the State except money in any State pension fund and money held under the State deferred compensation program.

Investment Guidelines and Management

The investment guidelines adopted by the Board provide, among other things, that no more than 10% of the portfolio may be invested in obligations of any one issuer other than the United States Government. Investments may be made only in fixed income instruments with maturities of up to five years in certain circumstances.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note B - Pooled Cash and Investments - Continued

Collateralization Requirements

All State funds are required by law to be collateralized by direct obligations of, or obligations which are guaranteed by the United States of America, or other suitable obligations as determined by the Board, unless the Board shall find such collateralization not in the best interest of the State. The Board has determined that certificates of deposit and time deposits must be collateralized unless the bank issuing the certificate has assets of not less than \$5 billion and is rated not lower and "B" by Fitch, Inc.'s Bank Watch Service. The Board has also determined that State's demand deposits need not be collateralized provided that any bank that holds these funds has for the last two years, a return on average assets of 5% or greater and an average equity - capital ratio of at least 1:20.

If the bank does not meet the above criteria, collateral must consist of one or more of the following:

- U.S. Government securities;
- U.S. Government agency securities;
- Federal Home Loan Board letters of credit;
- State of Delaware securities; or
- Securities of a political subdivision of the State with a Moody's Investors Service rating of "A" or better.

Since the Fund's pooled cash and investments are managed by the Treasurer, the Fund is unable to control compliance with the collateralization requirements or determine if these requirements have been met.

The policy is available on the Office of the State Treasurer website (<http://treasury.delaware.gov/>).

Pooled Cash and Investments - Federal Administrative Fund

The pooled cash and investments in the Federal Administrative Fund represent grant funds drawn to pay administrative expenses of the Fund. The grant agreement permits an amount up to 4% of grant revenues over the life of the program for these administrative expenses.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note B - Pooled Cash and Investments - Continued

Pooled Cash and Investments - Capital Reserve Loan Fund

The pooled cash and investments in the Capital Reserve Loan Fund represent all principal and interest received from Fund loans. These dollars are earmarked for future loans in accordance with applicable federal regulations.

Pooled Cash and Investments - Administrative Fees

The pooled cash and investments from administrative fees on municipal loans is recorded in the Nonfederal Administrative Fund, and is then available to the State for use at its discretion.

Note C - Loans Receivable

The loans receivable account is made up of the following major categories for the years ended June 30:

	<u>2016</u>	<u>2015</u>
Municipal loans		
Sussex County Council	\$ 44,450,307	\$ 48,427,252
City of Wilmington	37,835,733	37,681,603
City of Seaford	4,687,293	5,403,416
Kent County	19,889,214	21,510,614
City of Milford	1,418,735	1,560,698
New Castle County	2,251,415	2,057,273
Town of Selbyville	1,720,605	1,884,851
Town of Laurel	1,786,455	1,962,637
City of Dover	5,487,090	5,815,476
Camden Wyoming Sewer & Water Authority	126,847	137,203
Town of Millsboro	10,074,267	10,413,316
Town of Bridgeville	1,897,509	2,137,573
City of Lewes	8,147,690	8,776,920
Town of Delmar	996,678	1,027,342
Town of Georgetown	3,038,199	3,281,367
City of Harrington	4,641,272	2,750,518
Dewey Beach	270,837	316,973

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note C - Loans Receivable - Continued

	2016	2015
Municipal loans - continued		
Town of Middletown	274,535	295,968
Town of Smyrna	4,991,392	4,044,255
City of New Castle	-	28,364
City of Rehoboth Beach	383,119	428,037
Town of Harbeson	4,396,947	-
Total municipal loans	<u>158,766,139</u>	<u>159,941,656</u>
ARRA loans		
Sussex County Council	5,609,814	5,923,778
City of New Castle	-	20,415
Kent County	676,197	716,031
Total ARRA loans	<u>6,286,011</u>	<u>6,660,224</u>
State Agencies Loans	5,026,348	323,425
Septic Rehabilitation Program	2,803,404	2,863,027
Agriculture Nonpoint Source Loans	59,665	157,823
Dairy Loan Program	10,342	17,308
Expanded Agriculture Loan Program	<u>17,342</u>	<u>30,793</u>
Total loans	<u>\$ 172,969,251</u>	<u>\$ 169,994,256</u>
Current portion	\$ 9,942,352	\$ 10,959,431
Long-term portion	<u>163,026,899</u>	<u>159,034,825</u>
Total loans	<u>\$ 172,969,251</u>	<u>\$ 169,994,256</u>

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note C - Loans Receivable - Continued

Interest charged on these loans ranges from 0% to 6.0% for both fiscal year 2016 and 2015. Loan maturities vary, based on individual agreements. General Obligation and Municipal Revenue bonds are collateral for municipal loans; business assets and real estate are collateral for other loans.

The loans are shown net of an allowance for doubtful accounts of \$267,293 for fiscal year 2016 and \$203,850 for fiscal year 2015 for accounts in collection. During fiscal year 2016 and 2015, several loan balances were forgiven or written off as part of the terms of the loan agreements. Total loans forgiven or written off during fiscal year 2016 and 2015 were \$843,840 and \$1,203,904, respectively.

Note D - Significant Source of Revenue - State Revolving Loan Grant

The Fund currently derives a significant portion of its revenue from EPA State Revolving Fund Capitalization Grant awards and mandatory State matching funds. The total funds awarded through a series of agreements during the federal capitalization period (October 1, 1990 through June 30, 2016) were \$267,561,594, which includes the federal portion of \$226,174,510, or five-sixths, and the State matching portion of \$41,387,084, or one-sixth.

According to federal program guidelines, the Fund may spend up to four percent (4%) of the federal awards on administrative expenses. As previously described in Note A, a separate Administrative Fund is used to account for such costs and related revenues.

The table below summarizes funding for the Fund over the capitalization period:

	<u>Federal</u>	<u>State</u>	<u>Total</u>
Awards made through June 30, 2016	\$ 226,174,510	\$ 41,387,084	\$ 267,561,594
Awards expended through June 30, 2016	\$ 222,633,957	\$ 40,096,385	\$ 262,730,342

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note E - Deobligation of Federal Funds Between the Fund and the Drinking Water State Revolving Fund and Corresponding State Match

On September 4, 2012, the EPA deobligated \$27,050,177 of the Drinking Water State Revolving Fund (DWSRF) federal capitalization grant and awarded it to the Fund. As part of the deobligation, \$5,410,035 initially appropriated to the DWSRF, which represented the required 20% state match, was also appropriated to the Fund.

In accordance with the deobligation and the Fund's Intended Use Plan (Plan), the total \$32,460,212, described above, will be returned to the DWSRF when they are needed for Drinking Water commitments. The transfer will occur at management's discretion to facilitate cash flow for loan commitments incurred by DWSRF. When funds are transferred between the Fund and DWSRF, the funds will be accounted for as transfers out and in, respectively.

Note F - Pension Plan

Employees that administer the Fund are considered employees of DNREC and the State and are covered under the State Employees' Pension Plan (the Plan). While the Fund contributed to the Plan \$95,976 for fiscal year 2016 and \$105,352 for fiscal year 2015, respectively, which is included in the financial statements as personnel costs, the Fund is not a reporting unit and does not share in the State Employees' Pension Plan net pension liability.

Detailed information regarding the Plan is available in the Delaware Code and the Rules and Regulations of the Board of Pension Trustees. Certain significant Plan provisions include:

Plan Description and Eligibility - The Plan is a cost-sharing multiple employer defined benefit plan that covers virtually all full-time or regular part-time employees of the State, including employees of other affiliated entities.

Post-2011 Employee - Post-2011 employee shall mean an employee, as defined in 29 Del C., Section 5501(e), who is first employed by the State on or after January 1, 2012.

Service Benefits - Final average monthly compensation multiplied by 2.0% and multiplied by years of credited service prior to January 1, 1997, plus final average compensation multiplied by 1.85% and multiplied by years of credited service after December 31, 1996, subject to minimum limitations. For the Plan, final average monthly compensation is the monthly average of the highest three years of compensation.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note F - Pension Plan - Continued

For post-2011 employees, final average compensation per House Bill 81 shall include:

1. 1/36 of the compensation, minus overtime payments, paid to an employee during any period of 36 consecutive months or any 36 months comprised of three periods of 12 consecutive months in that employee's years of service credited under paragraphs (d)(1), (2), and #3 of this section in which that employee's compensation was highest, or the average monthly compensation paid to an employee during that period if such period is less than 36 months, plus
2. The dollar amounts of awards received under the "Teacher of the Year" and "Delaware Award for Excellence and Commitment in State Service" programs, plus
3. The total dollar amount of final lagged payments for credited service received by employees as defined under Section 2712 of Title 29.

Vesting - Five (5) years of credited service. For Post-2011 employees, ten years of credited service.

Retirement - Age 62 with five (5) years of credited service; age 60 with 15 years of credited service; or after 30 years of credited service at any age.

For Post-2011 employees, age 65 with ten years of credited service, exclusive of service credited under 29 Del C § 5501(d)(12); age 60 with 20 years of credited service, exclusive of service credited under 29 Del C § 5501(d)(12); or after 30 years of credited service at any age.

Disability Benefits - Same as Service Benefits. Employee must have five (5) years of credited service. In lieu of disability pension benefits, over 90% of the members of this Plan opted into a disability insurance program offered by the State effective January 1, 2006.

Survivor Benefits - If the employee is receiving a pension, the eligible survivor receives 50% (or 66.7% with a 2% reduction of benefit or 100% with a 6% reduction of benefit). If the employee is active with at least five (5) years of credited service, the eligible survivor receives 75% of the benefit the employee would have received at age 62.

Contributions - Employee - 3% of earnings in excess of \$6,000. For Post-2011 employees, 5% of earnings in excess of \$6,000. Employer contribution is determined by the Deferred Compensation Council.

Death Benefit - \$7,000 per member.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note F - Pension Plan - Continued

The State does not maintain the Plan information by agency and, therefore, the Fund's portion of the Plan's net position available for benefits, percentage of annual pension cost contributed, and the actuarial present value of vested and nonvested accumulated plan benefits is not readily available.

The Delaware Public Employees' Retirement System issues a publicly available financial report that includes financial statements and required supplementary information of the Plan. The financial report may be obtained by writing to the State Board of Pension Trustees and Office of Pensions, McArdle Building, Suite #1, 860 Silver Lake Boulevard, Dover, Delaware 19904-2402.

Note G - Commitments and Contingencies

1. Operating Lease

Beginning July 1, 1997, DNREC entered into a lease for office space, on behalf of the Fund, of which the Fund currently pays 100%. The operating lease is on a month to month basis. Rent expense, which is included in the financial statements as contractual services, was \$43,507 and \$39,552 in fiscal year 2016 and 2015, respectively.

2. Loan Commitments

The Fund has met its prior binding commitments (equal to at least one hundred twenty percent (120%) of each quarterly payment within one (1) year of receipt of that payment). As of June 30, 2016, there were binding commitments of \$38,779,513.

3. Cost Reimbursement Contracts

The Fund derives all of its non-operating revenue from EPA Capitalization Grants for State Revolving Fund Program and mandatory State matching funds which are contracts based on the reimbursement of allowance costs related to the program. Costs are subject to review by the EPA. Management does not believe there are any adjustments that could arise from disallowed costs that would materially impact the Fund's financial statements.

4. Deobligation of the Drinking Water State Revolving Loan Fund Grants

On September 4, 2012, the EPA deobligated \$27,050,177 of Drinking Water State Revolving Loan Fund (DWSRF) grant award and awarded those funds to the Fund. While the Fund is presently able to utilize those funds for its own projects, the funds will eventually be provided back to the DWSRF to fund drinking water projects in the future.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note H - Risk Management

The Fund is insured under the State's insurance plans. The State is exposed to various risks of losses related to workers' compensation, employee health-care and accident, automobile accident, police professional malpractice and property and casualty claims. It is the policy of the State not to purchase commercial insurance to cover these risks. Instead, State management believes it is more economical to manage its risk internally and thus, covers all claim settlements and judgments out of its General Fund.

The State continues to carry commercial insurance for all other risks of loss, including general liability and the remainder of the property and casualty liability. There have been no significant reductions in insurance coverage from prior years. In the past three years of insured coverage, settled claims have not exceeded commercial coverage.

Claim liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claim liabilities depend on such complex factors as inflation, changes in legal doctrines and damage awards, the process does not result in an exact amount. Claim liabilities are re-evaluated annually to take into consideration recently settled claims, the frequency of claims, and other economic and social factors.

At June 30, 2016, there were no outstanding or pending claims against the Fund.

Note I - American Recovery and Reinvestment Act of 2009

During the fiscal year ended June 30, 2009, the Fund was awarded additional funding as a result of the American Recovery and Reinvestment Act (ARRA) of 2009 in the amount of \$19,239,100. The Fund began processing various loan applications and began disbursing the funds in fiscal year 2011. The loan agreements state that each loan will be granted principal forgiveness of between 25% and 100% of the loan amount upon completion of the project. During fiscal year 2016 and 2015, the Fund forgave \$0 in ARRA loans.

Note J - Nonfederal Administrative Fund

The Nonfederal Administrative Fund account is used to supplement administrative expenses of the Fund and other water quality improvement expenses.

The Nonfederal Administrative Fund will also continue to fund the Septic Extended Funding Option (SEFO) Fund and other water quality areas. The SEFO Fund provides grants to individuals or entities which do not qualify for a Revolving Loan.

State of Delaware
Delaware Water Pollution Control Revolving Loan Fund

Notes to Financial Statements - Continued
June 30, 2016 and 2015

Note J - Nonfederal Administrative Fund - Continued

During the fiscal year ended June 30, 2016, the Nonfederal Administrative Fund funded the following:

SEFO grants	\$ 300,000
Wastewater matching planning grants	284,764
DNREC other program matching planning grants	754,247
Personnel costs for other water quality areas	<u>534,438</u>
Total	<u><u>\$ 1,873,449</u></u>

Note K - Subsequent Events

Events and transactions subsequent to year end have been evaluated for potential recognition in the financial statements or disclosure in the notes to the financial statements. All events and transactions have been evaluated through the date the financial statements were available to be issued.

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

To the Management
Delaware Water Pollution Control
Revolving Loan Fund
State of Delaware

We have audited, 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 the financial statements of the Delaware Water Pollution Control Revolving Loan Fund (the Fund) of the State of Delaware, as of and for the year ended June 30, 2016 and 2015, and the related notes to the financial statements and have issued our report thereon dated January 19, 2017.

Internal Control over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a 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 consider the deficiency described in the accompanying schedule of findings and responses as item 2016-01 to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free of 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*.

Fund's Responses to the Finding

The Fund's response to the finding identified in our audit is described in the accompanying schedule of findings. The Fund's response was not subjected to auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

This report is intended 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 the 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.

January 19, 2017

Gunnip & Company LLP

**State of Delaware
Delaware Water Pollution Control Revolving Loan Fund**

Schedule of Findings and Responses

Current Year Findings

Finding 2016-01: Continued Controls over Financial Reporting

Condition:

During the year, the Fund records its transactions on the cash basis of accounting using First State Financials (FSF), the State of Delaware's accounting system. In addition, the Fund's FSF accounts have been incorporated into QuickBooks for both internal and external reporting purposes. In connection with our audit, we noted that a formal and periodic reconciliation was not being performed between the amounts in FSF and QuickBooks for the Non Federal Administrative Fund. In prior year audits, the reconciliation was performed.

With some of the changeover in the personnel due to an unexpected medical emergency, procedures were not put in place to continue the necessary reconciliation process between FSF and QuickBooks.

Criteria:

In accordance with its methodology, Management needs to continue to ensure that all FSF and QuickBooks amounts are reconciled on a monthly basis and reviewed by the supervisor.

Cause:

With some of the changeover in personnel, procedures were not put in place to continue the necessary reconciliation process between FSF and QuickBooks.

Effect:

During the current year audit, we noted that current assets and change in net position were understated by approximately \$3.1 million.

Recommendation:

We recommend that management continue to reinforce the need for formal and periodic reconciliations between FSF and QuickBooks and that such reconciliations be reviewed by a supervisor.

**State of Delaware
Delaware Water Pollution Control Revolving Loan Fund**

Schedule of Findings and Responses

Management's Response:

Environmental Finance acknowledges the above audit finding and recommendation. The accounting position for the CWSRF and DWSRF programs has been filled. The incumbent has approximately 50 years of accounting related experience and extensive knowledge of FSF. The performance plan for the incumbent includes a requirement to review all completed monthly reconciliation reports with the Chief of Administration, obtain his signature, and to file the reports for annual audit review. In addition, the accounting processes and procedures for all reconciliation reports will be formally documented. To help support the overall accounting process, an Accounting Specialist has also been hired and is currently receiving FSF training.

Prior Year Finding

None outstanding.