



UNITED STATES ENVIRONMENTAL PROTECTION AGENCY
WASHINGTON, D.C. 20460

OFFICE OF WATER

MEMORANDUM

SUBJECT: Approval of Class Exception from the Clean Water and Drinking Water State Revolving Fund Cash Draw Rules

FROM: Raffael Stein, Director
Water Infrastructure Division

Anita Maria Thompkins, Director
Drinking Water Infrastructure Development Division

TO: Water Division Directors
Regions I-X

This memorandum announces a permanent regulatory exception (i.e., deviation) to the State Revolving Fund (SRF) cash draw rules. This class exception updates and modernizes the programs' federal cash draw rules. The Office of Grants and Debarment (OGD) approved this regulatory exception on November 18, 2022. This class exception will be in place until EPA can revise the existing SRF regulations.

This exception applies to the Clean Water State Revolving Fund (CWSRF) regulations at 40 CFR 35.3155(d)(5)(i) and (ii) and 40 CFR 35.3160(b)(2)-(4) and Drinking Water State Revolving Fund (DWSRF) regulations at 40 CFR 35.3560(f) and (g) and 40 CFR 35.3565(b). These regulations specify the rate at which states can draw federal funds in relation to state contribution. Further, the regulations slow the rate at which federal funds can be drawn for refinancing projects in the SRFs.

In plain language, this regulatory exception:

- Eliminates the requirement for states to draw SRF disbursement requests at a proportional federal to state ratio.
- Eliminates the cap on federal funds that can be drawn for refinance projects in the first eight quarters after EPA awards a capitalization grant to the state.

BACKGROUND

The CWSRF and DWSRF were established by amendments to the Clean Water Act (CWA) and the Safe Drinking Water Act (SDWA), respectively as financial assistance programs to protect and improve water quality and public health. The statutory requirements¹ for timely and expeditious expenditure of all funds in the CWA and SDWA direct states to efficiently use all financial resources in the programs to improve water quality and protect human health. The statutes do not specify cash draw requirements. In

¹ 33 U.S.C. §1382(b)(4) and 42 U.S.C. §300j-12(g)(3)

promulgating the programs' original regulations, the CWSRF and DWSRF programs set limits to the rate at which federal funds could be disbursed relative to state match contributions and for refinancing projects. For the CWSRF, the proportionality ratio was set at 83.33% federal, 16.67% state. For the DWSRF, the ratio depended on the amount of funds states took for set-asides and thus varied by capitalization grant. For refinancing projects, the regulation sets a ceiling for how much federal capitalization grant may be drawn to reimburse an assistance recipient in the initial eight quarters after award of the capitalization grant. While appropriate in the early years of the programs, these rules now serve as obsolete administrative burdens on the Agency's state partners.

Over recent decades, the CWSRF and DWSRF programs have adopted appropriate financial metrics to accommodate and conduct fiduciary oversight. This oversight includes EPA Project Officers ensuring that states properly deposit the state match into the fund at the time of or in advance of capitalization grant payments. The Intended Use Plan and Annual State Review checklists, used in the capitalization grant award process and annual review respectively, include items for EPA regions to confirm deposit of state match. Furthermore, EPA utilizes metrics such as fund utilization and disbursement ratios to holistically ensure states are disbursing funds in an appropriate and timely and expeditious manner. These metrics look at all sources of funding in an SRF, not only annual federal and state capitalization. The original cash draw rules established at the beginning of the SRF programs serve minimal utility for program oversight and are thus being eliminated.

IMPACT

Once Regions include the appropriate term and condition in new or already-awarded SRF capitalization grants (see Action section below), this permanent exception allows states to:

- Draw federal funds at a ratio of 100% for disbursement to assistance recipients to cover incurred project costs, and
- For a project that was funded through non-SRF municipal debt and is being refinanced by the CWSRF or DWSRF, allow the immediate expenditure of federal funds up to the completed portion of the project.

To align with industry-standard first in first out (FIFO) principles, states are encouraged to draw federal funds at a ratio of 100%, as this regulatory exception allows, after they have deposited the appropriate state match into the fund. However, states have the flexibility to continue their current cash draw processes (i.e., states may choose to continue proportional draws), after they have deposited the appropriate state match into the fund.

EPA HQ will modify the Annual State Review transaction testing procedure to reflect this class exception. EPA will no longer check proportionality on draws made from new capitalization grants going forward. For already-awarded capitalization grants that Regions amend (see Action section below), EPA will not check proportionality on draws made after the date of the respective grant amendment.

ACTION

Given that this class exception has the effect of a regulatory change, Regions must notify the states that the regulations cited above are no longer applicable. Regions must use the following term and condition in the award of all new SRF capitalization grants going forward. For this change to apply to already-awarded SRF capitalization grants, Regions must amend those grants to reflect this change with the

same term and condition. Until already-awarded capitalization grants are amended, they must comply with the cash draw rules governing the initial award.

Amended Cash Draw Proportionality

As of November 18, 2022, recipients are no longer required to comply with the cash draw rules in the Clean Water State Revolving Fund (CWSRF) regulations at 40 CFR 35.3155(d)(5)(i) and (ii) and 40 CFR 35.3160(b)(2)-(4) and Drinking Water State Revolving Fund (DWSRF) regulations at 40 CFR 35.3560(f) and (g) and 40 CFR 35.3565(b). If a grant that was awarded prior to November 18, 2022, is amended to include this term and condition, the recipient is no longer required to comply with the above-cited regulations. For further details on this change, see the notification memo from Division Directors Raffael Stein and Anita Maria Thompkins dated [Insert memo date] attached to this award.

The HQ SRF program offices are working with OGD to add this term and condition to the applicable funding recommendation templates in the Next Generation Grants System (NGGS). Further, the HQ SRF program offices will include these changes in each program's planned regulatory updates.

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