

66.468

DRINKING WATER STATE REVOLVING FUND

State Project/Program: DRINKING WATER STATE REVOLVING FUND

U. S. Environmental Protection Agency

Federal Authorization: Safe Drinking Water Act, Section 1452, as amended
Title 40 Code of Federal Regulations Chapter 1, Part 35, Subpart L

State Authorization: N.C. G.S. 159G

**NC Department of Environmental Quality
Division of Water Infrastructure**

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The auditor should not consider the Supplement to be “safe harbor” for identifying audit procedures to apply in a particular engagement, but the auditor should be prepared to justify departures from the suggested procedures. The auditor can consider the supplement a “safe harbor” for identification of compliance requirements to be tested if the auditor performs reasonable procedures to ensure that the requirements in the Supplement are current.

The grantor agency may elect to review audit working papers to determine that audit tests are adequate.

Auditors may request documentation of monitoring visits by the State Agencies.

This State compliance supplement must be used in conjunction with the OMB 2025 Compliance Supplement which is scheduled to be issued in May 2025. The OMB supplement will include “Part 3 - Compliance Requirements,” for the types that apply, and “Part 6 - Internal Control.” If a federal Agency issued guidance for a specific program, this will be included in “Part 4 - Agency Program”. The OMB Compliance Supplement is Section A of the State Compliance Supplement.

I. PROGRAM OBJECTIVES

The primary objective of the North Carolina Drinking Water State Revolving Fund (DWSRF) Program is to provide low-cost loans to potential applicants for public water supply systems infrastructure in order to achieve or maintain compliance with the Safe Drinking Water Act requirements and protect the public health objectives of the Act.

II. PROGRAM PROCEDURES

The Environmental Protection Agency (EPA) makes capitalization grants available to the State, which supplies a 20% match with State funds. The state DWSRF program obtains the capitalization grant by submitting an application for the noncompetitive grant to EPA including the Intended Use Plan (IUP). The IUP is a document that explains how the program will be administered for the upcoming year and goes through a public review period. Potential applicants may request DWSRF loan funds from the Division of Water Infrastructure (Division) in the North Carolina Department of Environmental Quality (DEQ). A number of steps are followed in determining which local governments receive funding.

- Potential applicants that wish to seek funding must complete an application package. Applications to the Division are reviewed and prioritized (i.e., ranked) based on information contained in the application, then presented to the State Water Infrastructure Authority (Authority) for approval.
- The Authority reviews the applications and staff ranking and then approves which projects are eligible for funding.
- Funding is subject to a schedule of deadlines and the Local Government Commission (LGC) approving the ability of the applicant to take on the project debt. The Division prepares the loan offer. Loans may be increased by 10% without additional LGC approval.
- Formal funding Award Offers are generated after the applicant meets such milestones as completing environmental review and obtaining approval of the engineering report. The Award Offer establishes the binding commitment date for funding, which is a reportable EPA project milestone. The project owner accepts several EPA conditions along with the loan terms by executing the Award Offer.
- The local units of governments submit bid packages to the Division, which then authorizes awards by approving a standard set of documents.
- The recipient executes a Notice to Proceed as part of the contract documents. The Notice To Proceed establishes the construction start date, which is also a reportable EPA milestone. Loan repayments are based on the “scheduled” completion date. Promissory notes and repayment invoices are generated by the LGC.
- During construction, requests for payment are made to the Division with accompanying invoices, which are reviewed and approved, by the program’s financial and technical staff. Modifications in the payment request are made for items over budget or contract or for ineligible costs. Any approved change orders are adjusted from the contingency budget. At 95% complete, the Division reviews the total project and can hold payments until requested items such as sale tax certifications, engineer’s certification on the project and certification of completion by the recipient have been received. The Certification of Completion states a date that construction was complete and accepted by the owner. This date is a reportable EPA project milestone. At project completion and final disbursing of funds, final loan repayment is set in coordination with the LGC.
- Interest accrues from the first disbursement of loan funds. The original date of completion in the construction contract establishes the first repayment date on either May 1 or November 1, whichever date is at least six months after original date of completion in the contract.

On November 15, 2022, the Bipartisan Infrastructure Law (BIL) (P.L. 117-58) was signed into law providing additional funding for the DWSRF with appropriations from 2022 through 2026. In addition to new grant funding base program activities, the law added two additional grants with one focused on funding Per and Polyfluoroalkyl Substances (PFAS) and emerging contaminants (EC) and one focused on Lead Service Line (LSL) removal. This supplement addresses compliance requirements for testing these funds.

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III. COMPLIANCE REQUIREMENTS

Noted below in the following matrix are the types of compliance requirements (Types) that are applicable to the federal program. These Types are either determined by the federal agency or the State Agency may have added the Type. This is noted by "Y." If the State determines that the federal requirement does not apply at the local level or if the State modifies the federal requirements, this is discussed in the supplement under the type of compliance requirement. If the federal and/or State agencies have determined that the type is not applicable, this is indicated by "N."

If the Type is applicable, the auditor must determine if the Type has a direct and material effect on the federal program for the auditee. The auditor must use the OMB 2025 Compliance Supplement, Part 3 and Part 4 (if an OMB supplement is issued) in addition to this State supplement to perform the audit.

A	B	C	E	F	G	H	I	J	L	M	N
Activities Allowed or Unallowed	Allowable Costs/Cost Principles	Cash Management	Eligibility	Equipment/ Real Property Management	Matching, Level of Effort, Earmarking	Period Of Performance	Procurement Suspension & Debarment	Program Income	Reporting	Subrecipient Monitoring	Special Tests and Provisions
Y	Y	Y	N	N	Y	Y	Y	Y	Y	N	Y

A. Activities Allowed or Unallowed

Compliance Requirements

Federal and State funds can only be expended for authorized projects as provided for in 40 CFR sec. 35.3520 and 35.3525 and further restricted by N.C.G.S. 159G.

Audit Objectives

Determine whether awarded funds were expended only for authorized projects.

Suggested Audit Procedures

The auditor should ascertain that activities have been limited to the construction of facilities as allowed by Safe Drinking Water Act, Section 1452, as amended and N.C.G.S. 159G.

B. Allowable Costs/Cost Principles

Compliance Requirements

Costs must be consistent with policies and procedures that apply to Federal/ State match program and other activities of the recipient organization. This includes guidelines and special conditions established by the agreement with the recipient. Allowable project costs are limited to the actual cost of the works described in the project application and indicated in the plans and specifications. Costs not allowed are expenditures for repairs, operation, and maintenance of any water supply system projects. Items not covered or allowed in the

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definition of “construction costs” as defined in G.S. 159G-3(4) are disallowed. For more details, see the EPA document, Drinking Water State Revolving Fund Program Rules, 40 CFR, August 2000.

Audit Objectives

Ascertain whether charges made to the awarded proceeds were for allowable costs.

Suggested Audit Procedures

Test a sample of transactions for conformance with the allowability of cost provisions of or limitations in the offer and the project review and cost summary document. Verify that costs are allowable.

C. Cash Management

All funds loaned pursuant to North Carolina General Statute 159G shall be expended solely for carrying out the approved project and an audit shall be performed in accordance with G.S. 159-34, as amended. The applicant will expend all of the requisitioned funds for the purpose of paying the costs of the project within three (3) banking days following the receipt of the funds from the State. Please note that the State is not a party to the construction contract(s) and the loan recipient is expected to uphold its contract obligations regarding timely payment.

Per 159G-37(b) – The Division of Water Infrastructure shall require all local governments applying for loans or grants for water or wastewater purposes to certify that no funds received from water or wastewater utility operations have been transferred to the local government's general fund for the purpose of supplementing the resources of the general fund. The prohibition in this section shall not be interpreted to include payments made to the local government to reimburse the general fund for expenses paid from that fund that are reasonably allocable to the regular and ongoing operations of the utility, including, but not limited to, rent and shared facility costs, engineering and design work, plan review, and shared personnel costs. (2005-454, s. 3; 2011-145, s. 13.3(kkk); 2013-360, s. 14.21(i); 2013-413, s. 57(u); 2014-100, s. 14.17; 2014-115, s. 17.)

Projects funded with Drinking Water State Revolving Funds are required to have Grant Project Ordinance in accordance with NC G.S. §159-13.2.

E. Eligibility

Not applicable

F. Equipment and Real Property Management

Not applicable

G. Matching, Level of Effort, Earmarking

The State is responsible for the matching requirements. No testing required.

H. Period of Performance

The State is responsible for the period of performance requirements. No testing required.

I. Procurement and Suspension and Debarment

Procurement:

Compliance Requirements

Follow federal procurement laws as applicable to federal awards found in the Uniform Guidance Procurement Standards (CFR §200.318 to §200.326). State procurement laws are found in G. S. 143-129, 143-131 and 143, Article 3, Public Contracts.

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Suspension and Debarment – Reference OMB Compliance Supplement Part 3 Compliance Requirements I. Procurement and Suspension and Disbarment.

Audit Objectives

Determine whether procurements were made in compliance with applicable Federal and State law.

Suggested Audit Procedures

Obtain the entity's procurement policies and verify that the policies comply with the compliance requirements found in applicable laws Federal and State laws were followed.

Test a sample of procurements to ascertain those applicable Federal and State compliance requirements found in the Uniform Guidance Procurement Standards (CFR §200.318 to §200.326) and NC G.S. §143 Article 8, Public Contracts.

Suspension and Debarment

Suggested Audit Procedures

1. Test a sample of contracts and ascertain if the required suspension and debarment certifications were received for subawards and covered contracts.
2. Test a sample of contracts to the List of Parties Excluded from Federal Procurement or Nonprocurement Programs, issued by the General Services Administration and ascertain if contracts were awarded to suspended or debarred parties.

J. Program Income

Compliance Requirements

Income can be obtained from Sales Tax refunds from Sales Taxes paid on purchases related to the construction phase of the project. The sales tax maybe elected to be reimbursed through the loan program or reimbursed from the state filing process for "Sales and Use Taxes".

Audit Objectives

Determine whether program income is correctly recorded and used in accordance with the program requirements.

Suggested Audit Procedures

Review the laws, regulations, and the provisions of the loan applicable to the program, and ascertain if the program income was anticipated and, if so, the requirements for recording and using program income

L. Reporting

Compliance Requirements

Recipient should use the Division's Request for Reimbursement form to request disbursement of funds.

Project costs incurred should be billed costs or disbursements and are in accordance with terms of the project. The reimbursements request represents the monies due which have not been previously received and that an inspection has been performed and all work is in accordance with the terms and conditions of the award.

Audit Objectives

Determine whether the Division's Request for Reimbursement form has been properly used, with supporting documentation, such as invoices, to report eligible expenditures.

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Suggested Audit Procedures

Perform appropriate analytical procedures to compare documented costs to accounting records and supporting documentation.

Compare a sample of previous reimbursement requested that have been approved by DEQ and determine if any subsequent reimbursements request represents the monies due which have not been previously received and that an inspection has been performed and all work is in accordance with the terms and conditions of the award.

M. Subrecipient Monitoring

Compliance Requirements

Implementing regulations for the DWSRF program are in 40 CFR part 35, subpart L. Subgrants are not available from the DWSRF program.

Potential applicants do not sub-award any monies to any sub-recipients and thus the State is monitoring the local governments as financial assistance recipients.

Testing is required at the local level.

N. Special Tests and Provisions

Compliance Requirements

All projects to which a loan or grant has been committed should be audited in accordance with G.S. §159-34 and G.S. §159-26(b)(6). A copy of the audit must be filed with the Department of Environmental Quality, Financial Services Division, unless a copy was submitted to the NC Department of State Treasurer, State and Local Government Finance Division. The Division will obtain a copy from DST.

Audit Objectives

Determine that the audit report agrees with the financial records of the recipient.

Suggested Audit Procedures

The statement of revenues and expenditures in the audit should agree to the accounting records. Please see Attachment A for a suggested format.

IV. OTHER INFORMATION

Please refer to the OMB Compliance Supplement, Part 4, No. 66, 66.458, Section IV. Other Information: DWSRF amounts are awarded by EPA to States as grants. The States then makes subawards in the form of loans to its subrecipients. Therefore, in determining the amount of Federal funds expended to be reported on the Schedule of Expenditures of Federal Awards (SEFA), subrecipients receiving DWSRF loans should include project expenditures incurred under these loans during the audit period as provided in 2 CFR section 200.502(a). These are subawards—not direct Federal loans—and, therefore, neither 2 CFR sections 200.502(b) nor (d) apply when calculating the amount of Federal funds expended.

Congress appropriated additional funds to the DWSRF in the Infrastructure Investment and Jobs Act of 2021, commonly referred to as the Bipartisan Infrastructure Law (BIL). The BIL appropriated additional funds for five fiscal years (FY2022-FY2026) for the Lead Service Line (LSL) program and Emerging Contaminants (EC program)

AUDIT REPORT

Project Description (Ex: Wastewater Facility)

Project Number

Municipality

For the Period _____ to _____

Statement of Revenues

Sources of Funds: \$ _____

Local (Cash)

Bond Sale Proceeds _____

State Funds _____

Federal Funds

Identify Federal Program
(grant or loan?) _____

Other Sources Identify _____

\$ _____

Statement of Expenditures

Construction Cost \$ _____

Contract I

Contract II

Engineering Fee _____

Administrative Expense

Identify _____

Legal Fees

Identify _____

Other

Land

Interest, etc. _____

\$ _____