



Legislative Fiscal Bureau

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Joint Committee on Finance

Paper #291

Revenue Obligation Bonding Authority (Environmental Improvement Fund)

[LFB 2021-23 Budget Summary: Page 184, #2]

CURRENT LAW

The environmental improvement fund consists of two state revolving loan funds, the clean water fund and the safe drinking water loan program. The clean water fund program provides financial assistance to municipalities for the planning, design, and construction of wastewater treatment facilities. Financial assistance is generally provided as a loan with an interest rate of 55% of the market interest rate for most project types. The safe drinking water loan program provides low-interest loans to municipalities for planning, designing, constructing, or modifying public drinking water systems, if the projects will facilitate compliance with national primary drinking water regulations under the federal Safe Drinking Water Act.

The U.S. Environmental Protection Agency (EPA) provides capitalization grants to provide capital to each loan fund to make financial assistance. The state is required to match 20% of the federal capitalization grants received. The state's match is provided through environmental improvement fund revenue bonds, with debt service paid from loan repayments. Under current law, EIF is provided with up to \$2,526,700,000 in revenue obligation bonding authority. The state match was previously provided through general obligation bonds, with most debt service paid through GPR. The clean water fund is authorized up to \$659,783,200 in general obligation bonds and the safe drinking water loan program is authorized up to \$74,950,000 in general obligation bonds.

DISCUSSION POINTS

1. Assembly Bill 68/Senate Bill 111 would increase environmental improvement revenue bonding authority by \$385,000,000. Total revenue obligation bonding authority for the program

would increase from \$2,526,700,000 to \$2,911,700,000. This would allow the state to provide the required 20% match for federal capitalization grants received as well as fund projected financial assistance needs for four fiscal years.

2. The environmental improvement fund is funded through federal capitalization grants and a required 20% state match. The biennial budget act has historically authorized the amount of bonds anticipated to be needed to provide the 20% match needed to maximize receipt of federal grants during that biennium. Any previously authorized but unused bonding authority is carried forward to the subsequent biennium. The federal government requires the state to have the entire 20% state match in place before it can accept federal capitalization grants.

3. The 2021-23 biennial finance plan issued by DOA and DNR and updated in March, 2021, estimates that the state will receive \$229.1 million in federal capitalization grant between federal fiscal year 2021 and 2025; this includes \$39.6 million in clean water fund capitalization grants and \$17.7 million in safe drinking water capitalization grants annually. On this basis, the state's required 20% match was estimated to total \$45.8 million during the four-year period covered by the biennial finance plan.

4. After the plan was published, the state was notified that it would receive \$42,955,000 in clean water capitalization grants and \$18,749,000 in safe drinking water capitalization grants in state fiscal year 2021-22. The amount of capitalization grants received in a given year varies based on factors out of the state's control, including federal appropriations. Therefore, it is not possible to predict how much capitalization grant funding the state will be eligible to receive in future years. DOA assumes that the state will receive the same amount of funding in each year of the 2021-23 and 2023-25 biennia, a combined \$61.7 million per year, or \$246.8 million over the four years considered in the biennial finance plan.

5. Federal rules generally require states to have 20% match funding secured before they may receive capitalization grants. AB 68/SB 111 would provide a 20% match sufficient to match projected \$229.1 million of federal grants over four years, rather than two, so that any potential delay in adoption of a state budget, or any increases in federal capitalization grants above estimated amounts, would not delay having sufficient state funding in place to accept the federal capitalization grants. Since the four-year projected capitalization grants increased to \$246.8 million, the state would be required to provide \$49,363,200 in match funding. The Committee could consider increasing EIF revenue obligation authority by \$49.4 million to provide the required state match on projected federal capitalization grants through state fiscal year 2024-25 [Alternative 1]. This would increase revenue obligation bonding authority from \$2,526,700,000 under current law to \$2,576,100,000.

6. Alternatively, the Committee could consider providing sufficient revenue bonding authority to provide the state's required match through only the 2021-23 biennium. Based on the federal fiscal year 2021 capitalization grants, the state is projected to be eligible to receive \$123,408,000 in clean water and safe drinking water capitalization grants over the next two fiscal years. To receive these grants, the state would be required to provide a 20% match of \$24,700,000 [Alternative 2]. This would increase environmental improvement fund revenue bonding authority from \$2,526,700,000 under current law to \$2,551,400,000.

7. If either Alternative 1 or 2 are adopted but actual federal grants were substantially higher than estimated, it is possible that some safe drinking water projects would have to wait to finalize financial assistance agreements until future biennia, or until subsequent legislation would authorize additional revenue obligation bonding authority sufficient to receive the future capitalization grants. Conversely, if actual federal grants were lower than estimated, any revenue bonding authority not needed in the 2021-23 biennium would carry forward to be available for use in future years.

8. In addition to the required state match, the EIF uses the proceeds of revenue bonds to fund any financial assistance agreements that cannot be funded through loan repayments and interest earnings or other fund incomes. The March, 2021, biennial finance plan estimated program demand for the clean water fund at \$799.8 million in the 2021-23 biennium and \$929.3 million in the 2023-25 biennium. Demand for the safe drinking water loan program is estimated at \$282.3 million in the 2021-23 and at \$335.4 million in the 2023-25 biennium. Total demand for EIF financial assistance is estimated to be \$1,082.1 million in the 2021-23 biennium and \$1,264.7 million in the 2023-25 biennium, as shown in the table.

Environmental Improvement Fund Projected Demand (Millions of Dollars)

	Percent of Market Interest Rate	<u>2021-22</u>	<u>2022-23</u>	<u>2023-24</u>	<u>2024-25</u>
Clean Water Fund					
	Pilot Projects (0%)	\$10.0	\$10.0	\$10.0	\$10.0
	0	18.8	20.3	21.9	23.6
	33	95.9	103.6	111.9	120.8
	55	241.9	261.2	282.1	304.7
	100	<u>18.3</u>	<u>19.8</u>	<u>21.3</u>	<u>23.0</u>
Total		\$384.9	\$414.9	\$447.2	\$482.1
Safe Drinking Water Loan Program					
	33%	\$60.1	\$65.5	\$71.4	\$77.8
	55	<u>75.0</u>	<u>81.7</u>	<u>89.1</u>	<u>97.1</u>
Total		\$135.1	\$147.2	\$160.5	\$174.9
EIF Total		\$520.0	\$562.1	\$607.7	\$657.0

9. In addition to the \$2,346.8 million in expected financial assistance agreements, the biennial finance plan anticipates that the EIF will need to fund \$26 million for program administration, \$407 million for debt service on general obligation bonds (issued prior to 2019) and revenue obligation bonds. With the projected capitalization grant match requirements of \$49.4 million, the fund is expected to use \$2,829.2 million between July 1, 2022, and June 30, 2025.

10. Under current projections, the EIF is expected to have \$1,843.3 million from federal grants, loan repayments, investments, fund equity, and other sources available to provide financial assistance. The fund also has \$610.5 million in authorized but unissued revenue bonding authority. Combined, these funding sources are expected to provide \$2,453.8 million available for the EIF. This leaves a projected gap of approximately \$375.9 million between estimated sources and estimated

financial assistance and other uses of funds. AB 68/SB 111 would provide \$385 million in revenue obligation bonding authority to fill this gap.

11. The Committee could consider providing \$375.9 million in additional revenue obligation bonding authority [Alternative 3]. This amount would provide sufficient funding to provide the state's required match for federal capitalization grants for four years (\$49.4 million) as well as fund estimated financial assistance agreements that cannot be funded through loan repayments through the 2023-25 biennium (\$326.5 million). This would increase revenue bonding authority for the EIF from \$2,526.7 million to \$2,902.6 million.

12. DOA reports that the \$610.5 million in authorized but unissued bonds would likely be sufficient to fund projected needs for financial assistance agreements through the 2021-23 biennium. As described above, increasing bonding authority for the program would provide sufficient funding for estimated financial assistance agreements in the 2023-25 biennium in case of delayed passage of the biennial budget. Without this additional bonding authority, the EIF could use only loan repayments and EIF interest earnings to fund financial assistance. Without sufficient funds, it is possible that some financial assistance may be put on hold pending the authorization of additional bonding.

13. Given available revenues and bonding authority, the Committee could take no action [Alternative 4]. As noted above, under current cash flow projections, the fund is estimated to have sufficient bonding authority to fund financial assistance agreements through the 2021-23 biennium. However, if federal grants are higher than projected there may be insufficient bonding authority to receive federal funding. Under this scenario, the EIF would likely be required to suspend closing on financial assistance under additional revenues can be provided.

ALTERNATIVES

1. Provide \$49.4 million in revenue obligation bonding for the environmental improvement fund, increasing bonding authority from \$2,526.7 million to \$2,576.1 million. (This would be estimated to provide sufficient funding for the state's required 20% match for capitalization grants received between fiscal year 2020-21 and 2024-25.)

ALT 1	Change to Base
BR	\$49,400,000

2. Provide \$24.7 million in revenue obligation bonding for the environmental improvement fund, increasing bonding authority from \$2,526.7 million to \$2,551.4 million. (This would be estimated to provide sufficient funding for the state's required 20% match for capitalization grants received between fiscal year 2020-21 and 2022-23.)

ALT 2	Change to Base
BR	\$24,700,000

3. Provide \$375.9 million in revenue obligation bonding for the environmental improvement fund, increasing bonding authority from \$2,526.7 million to \$2,902.6 million. (This would provide sufficient funding for the state's required 20% match for estimated capitalization grants received between fiscal year 2020-21 and 2024-25, as well as fund estimated financial assistance agreements that would not receive funding under current EIF income projections.)

ALT 3	Change to Base
BR	\$375,900,000

4. Take no action.

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