

# Guidance Document Chapter 3 – CWSP Financial Management

Act 76 of 2019 directed the Agency of Natural Resources (ANR) to assign by rule a Clean Water Service Provider (CWSP) to each watershed basin for the purposes of achieving pollutant reduction values and overseeing the identification, design, construction, operation, and maintenance of clean water projects within that assigned basin. To accomplish these goals, ANR, through the Department of Environmental Conservation (DEC), will issue Formula Grants to CWSPs. CWSPs will receive funds for identification, development and implementation of projects, operation and maintenance activities, Basin Water Quality Council (BWQC) coordination, and CWSP administration. ANR may also issue other awards to a CWSP, including start-up grants which will help prepare the CWSP to operate under its Formula Grant. CWSPs will be entrusted to manage grant funds, subject to DEC/ANR oversight. This chapter outlines the basic financial management expectations for CWSPs when administering formula, and where relevant, start-up and other ANR issued grants.

## **Chapter outline:**

- A. CWSP Financial Operations
- B. Internal Controls
- C. Procurement and Grant Issuance

### **A. CWSP Financial Operations**

- 1) Role of Management

DEC recognizes that CWSP operational management may pragmatically or formally be the responsibility of a staff member other than the executive director or manager of the entity assigned as a CWSP (i.e. the host entity). A host entity must formally designate to DEC one staff member as the “CWSP Director.” The CWSP Director may or may not be the host entity’s executive director/manager of the host entity.

The CWSP Director is accountable for compliance with all terms of applicable grant documents and implementation of the CWSP, including:

- Review and approval of the CWSP budget;
- Monitoring CWSP billing and expenditures;
- Preparing, verifying the accuracy of, and submitting CWSP financial and programmatic reports;
- Ensuring compliance with DEC oversight and re-appointment review activities;
- Ensuring compliance with internal controls procedures for CWSP activities;
- Ensuring CWSP compliance with applicable policies for staff members who perform work for the CWSP;
- Overseeing projects, whether or not another entity is subcontracted to manage that project;
- Overseeing Operation and Maintenance; and
- Communications with DEC, including early identification of any CWSP financial distress and barriers to implementation/meeting pollution reduction targets.

## 2) Solvency, Liquidity, Leveraging, and Program Effectiveness

The host entity for a CWSP must be solvent. To measure solvency, DEC will look primarily to see that CWSPs are not overly leveraged and that the host entity has sufficient cash flow to meet ongoing obligations, including payroll. DEC will do this by reviewing audited year-end financial statements of the host entity, monitoring other quarterly reporting as required by the formula grant, having conversations with CWSPs, conducting monitoring visits, conducting monitoring associated with the formula grant issuance process, and when reviewing a CWSP for reassignment.

Decreases in income, an increase in expenses, or cash-flow interruptions can all negatively impact solvency. The CWSP should promptly communicate to DEC significant changes that affect CWSP operations, especially changes to financial management-related staffing and program implementation. CWSP provision of effective and efficient services will require adequate staffing, however, CWSPs will not be expected to provide services that are not funded by the Formula Grant (or other grants). DEC considers the loss of staff, such that the separation of financial duties is impracticable or effective program implementation is stalled, as a concern warranting consultation with DEC staff.

## 3) Annual Review and Midway Review

DEC will work with CWSPs to conduct a programmatic audit and financial review once per year. This audit and review may involve a site visit that includes conversations with the CWSP Director and other staff working on CWSP operations, as well as conversations with the BWQC. DEC will also request documents from the CWSP as a part of this annual review, which will include audited year-end financial statements, when available.

Midway through a CWSP's five-year term, typically in year three, DEC and the CWSP may collaborate on a "midway review" of CWSP performance. The midway review is more extensive than the annual review, but less so than the CWSP reassignment application and review process in the final term year. The purpose of the midway review is to discuss progress with the CWSP in anticipation of the reassignment process.

In the last year of CWSP service, a CWSP in good standing may apply for reassignment for a new five-year term. More information on this process can be found in Chapter 10 of this Guidance Document.

## 4) Project vs. Administrative funds

Formula Grants are envisioned to contain authorization and sufficient liquidity for two uses of funds: 1) Project completion costs, and (2) administrative costs (also called program delivery costs in the CWIP funding policy). Funding for operations and maintenance of implemented projects will also be provided to a CWSP. O&M activities are covered in Chapter 7.

Project completion costs support costs associated with individual projects funded under the Formula Grant regardless of whether this work is sub-contracted or completed by the CWSP. Allowable costs include expenses incurred that directly relate to project identification, development, implementation and reporting of the individual project, including materials, travel, contracts, and personnel expenses for direct project implementation and management. Direct project management tasks may include stakeholder coordination, communications, procurement, development and monitoring of subcontracts, processing invoices for payment, overseeing and verifying project results, and preparing and compiling

grant deliverables. Per current DEC policy, project completion costs may include subcontractor/CWSP indirect costs. Project completion expenses are deducted from the project completion budget and not the program delivery (i.e. administration) budget. CWSPs should also consider including in their subgrant/procurement policies a section on allocation of administrative funds to subgrantees.

Administrative costs, described in the Clean Water Initiative's funding policy as "Program Delivery costs," supports costs associated with administering the operation of the CWSP and Formula Grant requirements, which may include the following. A CWSP's administrative costs are limited to 15% of the value of their overall Basin-specific allocation for Formula Grants. The 15 percent cap includes all expenses associated with program delivery, including indirect costs of program delivery and elements of subgranted program delivery work (if applicable). Examples include:

- Implementing a procurement policy (but not procurement activity related to a specific project);
- Staffing the BWQC, including meeting preparation and attendance;
- BWQC member expenses (for municipal and land conservation organizations);
- Managing the Formula Grant award;
- Maintaining the CWSP webpage/website
- Developing and monitoring subgrants and subcontracts;
- Processing subgrantee and subcontractor invoices for payment;
- Verifying project results (but not O&M which is in a separate category); and
- Preparing and compiling required grant deliverables (e.g., interim and final reports and project deliverables).

Administrative costs may include indirect expenses for the time spent on administrative tasks consistent with an entity's Negotiated Indirect Cost Rate Agreement (NICRA). CWSPs without a NICRA may be reimbursed for indirect expenses capped at 10% de minimis of their administrative fund allocation. See the CWIP funding policy for additional information.

## 5) Insurance

CWSPs shall comply with the insurance requirements contained in their Formula Grant awards, which are contained in the State's Attachment C template. Separate insurance for the CWSP is not required, assuming the host entity has insurance coverage that complies with Attachment C. CWSPs must provide proof of insurance coverage to DEC as part of executing a Formula Grant. In addition to the standard State insurance requirements, CWSPs will also be required to maintain/ensure the following insurance coverage for themselves and for their subcontractors or subgrantees as appropriate:

### a) Professional liability insurance.

Per the Clean Water Service Provider Rule (Vermont Environmental Protection Rules, Chapter 39), professional liability insurance is required for any professional services procured/paid for by a CWSP. Professional services include work performed by engineers, architects, lawyers, or accountants. The amount of professional liability coverage depends on the nature of the work performed, but typically should be procured minimally at \$1,000,000.00 per occurrence, and \$1,000,000.00 aggregate, although higher coverage is appropriate for larger projects.

b) Errors and Omissions.

The State recommends that CWSPs maintain standard Errors and Omissions insurance for the CWSP Director and BWQC members. This insurance may be paid for from 'Administrative Funds'. Coverage should be minimally in the amount of \$1,000,000.00 per occurrence, and \$1,000,000.00 aggregate. The State will not be responsible for any losses associated with the failure to procure this coverage.

c) Performance bonds for projects

Performance and payment bonds shall be required for projects over \$500,000.00 in value, while performance bonds are recommended as best practice for projects in excess of \$250,000.00 in value. Contractors may add the cost of the bond to their overall fee, which in turn may be paid for by the CWSP using "project funds."

It is recommended that CWSPs require subcontractors and subgrantees to obtain insurance at the level required by Schedule C of the standard State grant/contract. However, when a CWSP hires a project developer as a subcontractor to oversee design or construction of a clean water project, including any operation and maintenance work, that subcontractor shall be required to obtain the standard insurance coverage expected of grantees and contractors who sign agreements with the State.

6) Investment of CWSP funds; Insurance on CWSP funds.

CWSPs shall deposit all CWSP related funds, including both program, administrative and operations and maintenance funds, into Federal Deposit Insurance Corporation (FDIC) or National Credit Union Administration (NCUA) insured savings or checking accounts at an accredited financial institution or with the State Treasurer, if applicable. All funds deposited with a bank or credit union must be insured; should balances exceed the insured maximums, the CWSP shall make sure to create a sweep account process, create a second account, or other mechanism to ensure the funds are always insured.

Funds shall not be deposited into any other accounts, including money markets, CDs, or any other investment without prior written approval from DEC.

7) Leftover Funds

Act 76 states that once a CWSP is deemed to have met their pollution reduction goal, or five-year target, and has excess formula grant funds available, a CWSP may:

- a) Carry those funds forward to the following year;
- b) Use those funds for other eligible projects;
- c) Use those funds for operation and maintenance responsibilities for existing constructed projects;
- d) Use those funds for projects within the basin that are required by federal or state law; or,
- e) Use those funds for other work that improved water quality within their assigned basin, including river corridor protection, aquatic species passage, or other similar projects.

Per statute, the CWSP decides how to spend leftover funds. However, should the CWSP decide to spend Leftover Funds on other eligible projects, that decision must be advanced to the BWQC, for approval before any funds are expended on said project. Should a CWSP decide to spend Leftover Funds on O&M,

or to carry those funds forward to the next year, instead of advancing a project, the CWSP may seek input and counsel from the BWQC, although, the CWSP has the final say on this matter.

Also, because spending formula grant funding on anything besides non-regulatory projects may impact a CWSP's (and relatedly the State's) ability to meet future non-regulatory pollution reduction targets should that CWSP be re-assigned to serve in their basin, a CWSP can only use left-over funds for other uses besides non-regulatory project development if the Clean Water Fund has fully funded formula grants sufficient to meet the entirety of the non-regulatory load allocation requirements of a TMDL in a given basin. In other words, if funding was not sufficient, a CWSP would be able to either carry forward Left Over Funds into the future, spend them on other eligible non-regulatory projects, or spend the funding on Operations and Maintenance of constructed non-regulatory projects to retain or extend their phosphorus reduction capabilities.

More on projects can be found in Ch. 6.

#### 8) Risk Reserve

The idea of a risk reserve was first discussed with the Act 76 advisory group, as a way to manage situations where a CWSP has incurred costs, but due to acts outside the control of the CWSP (such as weather, or acts of a third party), a project is damaged or destroyed.

The recommendation to appropriate a risk reserve from within the Clean Water Fund is subject to a decision by the Clean Water Board. The Board, in recommending its annual budget, already maintains a contingency reserve unrelated to CWSP project risk of loss. Should the Board decide to fund a risk reserve, it would be subject to the following considerations:

- a. Access. The Secretary shall make the final decision on whether a CWSP qualifies for funding from the risk reserve, subject to the eligibility provisions of Act 76.
- b. Amount. Any funds will be limited to actual damage to the project, so that the project can be rehabilitated.
- c. Process. The Department shall provide a form for CWSPs to use to apply for Risk Reserve funding.

If appropriated, DEC will hold and administer the risk reserve. Authorization to access risk reserve funds will be contained in a CWSPs' formula grant, subject to approval by the State. A separate risk reserve policy may be developed, providing guidance for when and how the risk reserve may be accessed.

#### 9) Reporting

CWSPs are responsible for reporting on programmatic, organizational, financial, and grant-related information. Specific reporting requirements are contained throughout this Guidance and will be referenced in a CWSP's start-up and Formula Grant awards. DEC will provide CWSPs a form to aid the management of reporting requirements.

CWSPs must retain records and provide for site access to ANR. Please see Chapter 2, for more information on the records retention and site access requirements for CWSPs.

#### 10) Other revenue sources

Formula Grants cannot be used as match for any other grant, without prior written approval from DEC. CWSPs may access other funds and use them to improve water quality. The availability of additional funding shall not change or impact any requirements for how a CWSP uses its Formula Grant. The effect of co-funding on pollution accounting for a CWSP is covered in Chapter 6.

## **B. Internal Controls**

Internal controls are the policies, processes, and procedures used to ensure accountability in the management of financial information and transactions. CWSPs are expected to follow internal controls, which must be documented in an internal controls Policy, that is subject to DEC review and approval.

### 1) Requirements, Submission and Approval, Updates

Per Environmental Protection Rule § 39-306(f), CWSPs shall maintain an adequate Internal Controls policy, that at least addresses separation of duties for financial activities, use of an electronic accounting system, budget reconciliation, tracking of staff time spent on grants, procurement procedures, authorizations for purchasing and procurement, written accounting procedures, financial reporting, personnel policies, and safeguarding of assets. CWSPs must file their internal control policies with DEC prior to receiving formula grant funding.

Internal control policies should be kept up to date and adhered to. Once every five years, CWSPs should review their Internal Controls policies and processes to ensure they meet sufficient, evolving best practices. DEC recommends that this review take place in year three of a CWSP's five-year term. CWSPs should review their own compliance with the Internal Controls policies and procedures at least once per year. Furthermore, DEC may require CWSPs to complete an Internal Controls Self-Assessment once every three years.

### 2) Internal Controls Policy and Procedure Components

#### a) Separation of duties (paying invoices, approvals, check issuance, reconciliation)

The segregation/separation of duties is a well-established principle of any internal controls policy. The policy achieves two major goals: It provides for review and oversight to catch errors, and it helps deter and prevent fraud/theft.

Three key duties should be separated between three separate employees: custody of assets (including financial accounts) and accounting/recordkeeping, authorization of use of the assets (i.e. signing checks, approving procurement), and reconciliation.

#### b) Electronic Accounting System

Some firms still keep track of their financial transactions in whole or in part in a manual, paper-based ledgers. This is not allowed for CWSPs, who must keep track of their financial transactions using a computer-based accounting program.

#### c) Reconciliation

Reconciliation of CWSP formula funds should be performed frequently, but by a separate staff member from the person who is the custodian of assets, the financial staff member recording transactions, or the CWSP Director.

d) Staff time tracking

Each CWSP will have systems and processes in place to accurately track staff time worked by formula award, fund type (administrative vs. project funds) and project (if and when staff charge time to project funds). Tracking shall be accurate, and timesheets/records shall be kept and retained, and be available for review upon request by DEC.

e) Authorizations – purchases/procurement (goods and services); task order approvals

CWSPs should identify staff members who are authorized to approve purchasing and/or expenditures of CWSP funds in a policy.

Authorization to expend funding must be consistent with the other provisions of Act 76, including BWQC approval, and contracting/documentation requirements with contractors/grantees. Authorizations, including any delegations of authority should be made in writing.

f) Accounting

CWSP funds shall be accounted for as a separate fund on all CWSP host entity financial reports.

g) Financial Reporting

Quarterly draw requests under formula awards will be accompanied by a quarterly Balance Sheet, and a Profit/Loss or equivalent statement showing expenditures of CWSP formula funds.

Yearly, CWSPs shall submit year end, audited financial statements for the entity serving as the CWSP to the Department. Financial statements shall show activity by fund, including activity of the CWSP. If applicable, CWSPs shall also submit a Form 990 to DEC. All year-end reports should be submitted to the Department within 180 days of the end of their fiscal year.

### **C. Procurement and Grant Issuance**

In collaboration with the BWQC as noted herein, CWSPs shall have discretion to issue and distribute subgrants and subcontracts for clean water projects pursuant to the requirements of this Guidance document and the Clean Water Service Provider Rule, Chapter 39. In such cases, potential subgrantees and subcontractors will apply directly to the CWSP for grant and contract RFPs authorized by the BWQC.

1. Procurement Considerations for CWSPs

a. Requests for Proposals

Competition in the procurement process and grant issuance process serves both the State, CWSPs, and potential bidders by ensuring the process produces an optimal solution at a reasonable price and allowing qualified vendors and grantees an opportunity to obtain CWSP business and awards. In addition to complying with existing statutory and regulatory requirements, CWSP procurements for both subcontracts for services and subgrants (from entities that are NOT pre-qualified by the CWSP) should consider the following general best practices:

- Prepare written specifications in the form of a Request for Proposal (“RFP”) when soliciting bids. Elements that should be included in the written specification include:
  - A Statement of Work to be performed;
  - Programmatic, performance, and financial requirements/measures;
  - Expectations regarding service location, schedule, including deadlines for deliverables and/or milestones, if applicable;
  - Payment provisions for all phases of work to be performed, including maximum award amount (e.g. performance based deliverables and/or hourly rates that apply to all phases of work);
  - Other specific State requirements or conditions;
  - Criteria for selection.
- To comply with the Rule, solicit price quotations from 3 or more qualified vendors, when soliciting services. Posting the RFP to the public is a recommended best practice but is not appropriate for all solicitations. All communications with the vendors to obtain price quotes must be documented (emails, fax, notes from phone calls, etc.). Solicitation may be open, or limited to a category of pre-qualified entity, see (b), below;
- Solicitations for services should not place unreasonable requirements on firms that affect the competitive nature of the procurement process.
- The vendors solicited should understand they will be required to sign an agreement that includes provisions of the formula grant that are required to be passed onto subcontractors/subgrantees, together with other applicable requirements;
- All records relating to the RFP/bid process, including proposals and a record of the selection process, shall be retained in the contract/grant file in accordance with the CWSP’s records retention schedule;
- The quotation most responsive to the selection criteria should be selected;
- Criteria selection should include cost and qualifications. Other criteria can also be used, including timing and familiarity with the work/project.
- Where feasible, procurements should be reviewed by at least three members of the CWSP as a best practice.
- BWQC members may not participate in procurement decision making.



b. Pre-Qualification of Entities and Sole Sourcing

Use of “Sole Source” or “no-bid” Contracts or Grants is contrary to the competitive process supported by the State. The Act 76 Rule prohibits sole sourcing in most circumstances. Sole Source subawards are allowed when an entity has been prequalified to provide services pursuant to § 39-306(h) and whose clean water project has been selected pursuant to § 39-403(e). The only entities who meet these criteria will be providing project management services. Engineers and providers of operations and maintenance services are not considered entities that ‘have a clean water project.’

Pre-qualification is a process, however, that is open to other types of services beyond ‘project managers.’ More specifically, pre-qualification is a tool that a CWSP might employ to simplify procurement by retaining a pool of qualified providers that can be solicited as the need arises. Typical categories of services that a CWSP might seek pre-qualified entities for include engineering, project management, and construction, among other examples. CWSPs may run a competitive procurement that only solicits entities from their list of pre-qualified entities, provided there are more than two pre-qualified entities in a given category of service provider (e.g. 3 engineering firms, 3 green infrastructure construction firms, etc.). Pre-qualification alone does not remove the requirement for CWSPs to issue a competitive RFP and follow a competitive procurement process.

A CWSP should document their pre-qualification requirements in their subgrant/ procurement policy, that includes the process, standards and criteria that must be met, in order for an entity to be considered ‘pre-qualified’ in a given category. This policy should also document what an entity must do to stay ‘pre-qualified.’ At a minimum, a CWSP shall open up the pre-qualification process to new entities at least once per year. CWSPs may consider the cost of work when procuring services, even from a pre-qualified entity. The decision to issue a sole source agreement should be documented in a memo that is signed by the CWSP Director and kept in the grant/contract file.

Certain relevant master contracts entered into by the State Department of Environmental Conservation with a contractor may de facto pre-qualify that vendor for procurement with by CWSP under this Guidance Document]. Contracts for work on river corridor easements are the main example for this type of arrangement. More on what constitutes a ‘relevant’ master contract for these purposes can be found in Chapter 6.

c. Pre-qualified Project Managers

The State recognizes that many projects will be brought to the attention of a CWSP as a result of the preparation and groundwork of external partners, including watershed and conservation groups. A partner watershed or conservation group that has developed a project will be in a competitive position to be procured as a project manager (i.e. implementer) for the project that they bring forward for consideration, if they are cost competitive, due to the relationship that they have with the landowner and/or unique knowledge that is key to implementing a project without which, the project might not proceed. CWSPs that do not procure the watershed or conservation group that

developed a project as the project manager may be burdened with additional costs, both real and intangible, which may challenge the viability of a project, up to and including sunk investment. For these reasons, when a project is selected by a BWQC, the CWSP is encouraged to use its authority to sole source and assign that project when the originating organization of that project is a prequalified project manager. A CWSP might not issue a contract to the prequalified entity, however, if the entity is debarred, if there is a conflict of interest, if the costs are unreasonable, or if there are other reasonable concerns related to performance.

d. Debarment

As part of the procurement process, the CWSP must confirm that any vendors they procure must not be debarred. The State has created guidance on how grantees, including CWSPs, can perform debarment checks. The current guidance can be found at this link: <https://dec.vermont.gov/funding/DEC-grant-resources/state-federal-resources>. The State will conduct occasional spot checks to audit whether vendors are accurately reporting their debarment status to CWSPs. CWSPs are encouraged to do the same.

e. Procurement and Conflicts of Interest

Employees with a conflict of interest or appearance thereof, should not participate in, control or influence the bidding process, the awarding of contracts, or the approval of payments against said contracts. Further, it is recommended that CWSPs should require every subcontractor/subgrantee to disclose in writing any actual or potential conflict of interest. Anyone with an appearance of a conflict of interest should disclose that conflict in a timely manner.

Basin Water Quality Members that vote to approve (or deny) to advance a project are generally considered conflicted for the purposes of participating in the administration of that project, and, depending on the situation, may not be eligible to bid on any procurement or receive funds as a subcontractor or subgrantee on that project. Should a BWQC member so-conflicted wish to respond to bid on a procurement offering by the CWSP for that project, the conflict created by the prior vote shall be disclosed and a determination of eligibility made by the CWSP.

## 2. Role of the BWQC in Procurement

The State does not view Act 76 as providing the BWQC with the authority to make decisions on the procurement of goods and services necessary to accomplish clean water projects. Therefore, the BWQC should not participate in the review of procurements by the CWSP. BWQC decision-making in procurement exacerbates potential and real conflict of interest issues and should be completely avoided. The CWSP may request input from a BWQC member **who is not conflicted** (e.g. for a reference, or on a procurement review team) as appropriate.

Moreover, the BWQC process of selecting projects is not the same as procurement, and BWQCs do not procure or pick implementers when picking a project. CWSPs alone are responsible for procurement under the formula grant. The CWSP as the administrator of the formula grant needs to have discretion

on how to proceed (i.e. discretion over means/methods) in order to achieve their phosphorus targets in a cost-effective manner, which is their essential responsibility to the State. A CWSP needs this discretion in order to comply with applicable rules and laws (e.g. debarment), which is their charge, as well as to ensure the implementation of cost-effective and technically effective projects, which authority also includes termination of subgrants and subcontracts.

Removing procurement decisions from the CWSP would undermine a CWSP's ability to achieve their assigned phosphorus reduction goal by requiring the selection or retention of a specific implementer, regardless of cost, quality, debarment status, or despite mid-project problems from the procured party. With responsibility for achieving a phosphorus reduction goal, a CWSP must have tools that they can use to manage costs and quality of projects.

Finally, if a BWQC was voting on procurement, each BWQC member who was proposing a project in any given meeting would have to recuse themselves from the entire meeting if/when requests for funding exceeded available funding. This dynamic was discussed by the advisory group during development of the Rule where it was deemed to be fatally problematic for the operation of the BWQC and was rejected by the group.

### 3. Procurement of Goods and Asset Management

When procuring goods, where an item is valued at \$1,000.00 or above, two bids must be solicited and documented. The only exception is when it is impossible to get two bids because the good in question is proprietary and is only available from one vendor. When this occurs, this should be documented to the file. Records related to procurement of goods shall be retained for at least one year after the audit covering the procurement. Records related to procurement of services shall be retained for at least three years after the audit covering the procurement. Procurement of a good or category of goods totaling \$15,000.00 or greater from one vendor in one year shall be by written contract.

CWSPs may choose to spend money on equipment and other tangible assets in the course of their service, to facilitate implementation of pollution reduction projects. All equipment and tangible assets shall be maintained, as appropriate. CWSPs shall follow the terms of their Formula Grant when disposing of assets purchased with grant funds.

### 4. Monitoring of subcontracts and subawards by the CWSP and Procurement/subgrant guidance

CWSPs should consider the best practice of monitoring their subgrants for compliance with the terms of their award.