

**Underground Storage Tank Indemnification Fund
Interim Financial Report
(Unaudited)**

For the Fiscal Years Ended June 30, 2017 and 2016



Prepared By:

Office of Comptroller Operations
Bureau of Accounting & Financial Management

**Underground Storage Tank Indemnification Fund
Financial Statements
(Unaudited)
For the Fiscal Years Ended June 30, 2017 and 2016**

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**Underground Storage Tank Indemnification Fund
Statement of Fiduciary Assets and Liabilities
(Unaudited)
As of June 30**

	2017	2016
ASSETS:		
Deposits and Investments— Note B		
Cash-In-Transit.....	\$ 300	\$ -
Temporary Investments.....	11,790,524	13,619,414
Long-term Investments.....	236,461,460	208,829,238
Receivables— Note C		
Interest on Loan to General Fund.....	15,132,858	14,588,915
Investments Interest and Dividends.....	946,246	894,002
Investments Sold.....	561,566	1,419,763
Advances to Other Funds— Note D.....	67,500,000	67,500,000
TOTAL ASSETS	<u>\$ 332,392,954</u>	<u>\$ 306,851,332</u>
LIABILITIES:		
Payables— Note E		
Accounts Payable and Accrued Liabilities.....	\$ 15,275,853	\$ 15,611,910
Invoices Payable.....	2,164,147	1,925,852
Investments Purchased Payable.....	1,153,682	3,075,105
Due to Other Obligations— Note F.....	256,484	241,258
Other Liabilities— Note G.....	313,542,788	285,997,209
TOTAL LIABILITIES	<u>\$ 332,392,954</u>	<u>\$ 306,851,332</u>

- The notes and supplemental schedule to the financial statements are an integral part of this statement. -

**Underground Storage Tank Indemnification Fund
Statement of Receipts and Disbursements
(Unaudited)
For the Fiscal Years Ended June 30**

	2017	2016
RECEIPTS— Note H		
Fees:		
Gallon.....	\$ 52,461,700	\$ 52,229,410
Tank Capacity.....	6,209,734	5,938,478
TIIP.....	327,380	299,230
Investment Income:		
Interest and Dividend Income.....	5,223,182	4,725,169
Recapture of Broker Commissions.....	4,736	18,759
Net Increase in Fair Value of Investments.....	12,015,021	1,090,384
Interest on Loans.....	543,943	234,501
Litigation Settlement.....	-	544,945
Other Receipts.....	15,771	350,207
TOTAL RECEIPTS.....	<u>76,801,467</u>	<u>65,431,083</u>
DISBURSEMENTS— Note H		
Administrative:		
Insurance Department Personnel and Other Charges.....	657,227	(947,332)
Third Party Administrator.....	4,759,325	5,234,284
Professional Services.....	1,312,930	1,475,731
Loan Administration.....	-	(640)
Total Administrative.....	<u>6,729,482</u>	<u>5,762,043</u>
Claims Indemnification:		
Losses.....	33,661,661	36,424,186
Loss Expenses - Non-Legal.....	2,243,460	2,260,406
Loss Expenses - Legal.....	304,497	330,954
Total Claims Indemnification.....	<u>36,209,618</u>	<u>39,015,546</u>
Allocations - Funds Released:		
Environmental Cleanup Program.....	2,951,448	2,997,369
Pollution Prevention Program.....	42,811	62,660
Catastrophic Release Program.....	13,080	39,199
Investigation and Closure Costs.....	2,954,313	3,355,192
Total Allocations - Funds Released.....	<u>5,961,652</u>	<u>6,454,420</u>
TOTAL DISBURSEMENTS.....	<u>48,900,752</u>	<u>51,232,009</u>
NET RECEIPTS OVER (UNDER) DISBURSEMENTS.....	<u>\$ 27,900,715</u>	<u>\$ 14,199,074</u>

- The notes and supplemental schedule to the financial statements are an integral part of this statement. -

NOTE A - Summary of Significant Accounting Policies

Basis of Presentation

In order to provide information useful to management, the financial statements for the Underground Storage Tank Indemnification Fund (USTIF) are reported utilizing an economic resources measurement focus, and an accrual basis of accounting. These statements are not fully in compliance with U.S. generally accepted accounting principles (GAAP) applicable to state and local governments as the Statement of Changes in Fiduciary Assets and Liabilities has been excluded from this report and the Statement of Receipts and Disbursements is presented in order to meet the needs of management. Under this basis, all assets and liabilities are included regardless of when cash is received or payment is disbursed. Receipts are recognized in the fiscal year earned and Disbursements are recognized in the fiscal year incurred.

The content of this report is intended solely for internal management purposes.

Financial Statements

The financial statements report the fiduciary assets and liabilities and receipts and disbursements for the fiscal years ended June 30, 2017 and 2016. The Statement of Fiduciary Assets and Liabilities is a summary of financial balances at a specific point in time. Assets and liabilities are presented as of a specific date, generally at the end of a closed period or fiscal year. The Statement of Receipts and Disbursements presents increases (i.e., fees and investment income) and decreases (i.e., disbursements) in fiduciary resources.

Fund Structure

Fund Accounting: In governmental accounting, a fund is defined as an independent fiscal and accounting entity, with a self-balancing set of accounts, recording cash and/or other resources together with all related liabilities and equities which are segregated for the purposes of carrying out specific activities or attaining certain objectives in accordance with the fund's special regulations, restrictions or limitations. In the Commonwealth, funds are established by legislative enactment or, in certain rare cases, by administrative action.

Financial Reporting Entity

The Storage Tank and Spill Prevention Act, Act 32 of 1989, as amended, established the USTIF to administer a program to provide claim payments to owners and operators of underground storage tanks who incur liability for taking corrective action, bodily injury or property damage caused by a release from underground storage tanks. The cost covered by the USTIF includes identifying the extent, nature and impact of the release and develops a remedial action plan for restoring the site. The USTIF will not cover any upgrade costs for the facility or any repair and maintenance work performed on the underground storage tanks, including tank removal. Administrative disbursements of the fund are also covered. The fund is administered by the Insurance Department in conjunction with the nine member Underground Storage Tank Indemnification Board.

Act 13 of 1998 established a new loan program to assist owners of regulated underground storage tanks to upgrade their underground storage tank systems to meet federal Environmental Protection Agency upgrade requirements or to remove them from service. Act 100 of 2000 expanded the upgrade loan program to include the removal of underground storage tanks. The act also established an environmental cleanup program and a pollution prevention program that are administered by the Department of Environmental Protection.

Measurement Focus and Basis of Accounting

For financial reporting purposes, USTIF is classified as a fiduciary fund and as such consists of assets that are held in trust and that a government cannot use to the benefit of its own programs. USTIF is considered an agency fund type. Agency funds typically involve the receipt, temporary custody and remittance of resources to specific individuals, private organizations or other governments, and thus do not report equity balances.

The financial statements are prepared using a full accrual basis of accounting and economic resources measurement focus. Balances are presented utilizing data posted to the Finance (FI) module of SAP to include accruals—or all subsequent activity—applicable to the reporting period, regardless of when cash is actually received or disbursed.

Beginning with the report for the fiscal year ended June 30, 2016, all long-term liabilities, including net pension and related items and accruals for self-insurance, compensated absences and other postemployment benefits have been eliminated. In consultation with the GASB and other sources, a reexamination of the governmental arrangement of agency funds revealed that long-term liabilities should be excluded as fund obligations. Agency funds are used to report resources held by the government in a purely custodial capacity. Since there is no specific resource being held to cover these long-term liabilities and related deferred items, such items should not be reported in the agency fund but shall be reported in the General Fund.

Normal Balances

A normal balance is the expectation that an account will have either a debit or a credit balance based on its classification within the chart of accounts. It is possible for an account expected to have a normal balance as a debit may actually have a credit balance, and vice versa, but these situations should be minimal. An abnormal balance is typically reported as a negative value on the face of the financial reports and explained within the notes.

NOTE B - Deposits and Investments

Pooled Cash

In accordance with the Fiscal Code, cash balances of most Commonwealth funds are pooled by the Treasury Department. Cash balances are accounted for centrally for receipt and disbursement purposes and are segregated by fund. These cash deposits facilitate daily transactions on behalf of the funds and are maintained separately from the investment fund balances. The law requires that collateral be pledged by banks and other financial institutions to guarantee cash on deposit.

Cash-In-Transit as of June 30, 2017 and 2016 consist of \$0.3 thousand and \$-0-.

Treasury Investment Pools

The deposit and investment policies of the Treasury Department are governed by Sections 301, 301.1 and 505 of the Pennsylvania Fiscal Code (Act of 1929, P.L. 343), and Section 321.1 of the Pennsylvania Administrative Code (Act of 1929, P.L. 177, No. 175).

In compliance with the Fiscal Code, the Treasury Department holds investment control over the USTIF and most other funds of the Commonwealth. The Treasury Department uses a variety of internal investment pools that seek to provide preservation of principal, liquidity, diversification, and income for most funds. All participating funds report amounts invested in such pools as Temporary or Long-term Investments.

The Treasury Department manages the Commonwealth Investment Program (CIP) for funds that are part of the primary government. Investments in the CIP are reported as shares by the participants. Investments are reported at fair value, typically using published market prices.

Temporary Investments are those investments expected to be realized in cash within twelve months or less following the reporting period and Long-term Investments are expected to be realized in cash beyond one year. The Treasury Department accounts for the investments held in the CIP for each participating fund's equity (considered shares) on a daily basis. Share balances of participating funds may fluctuate considerably during the fiscal year, based on the timing of cash receipts and disbursements in the participating fund. Periodic earnings of the CIP are allocated to specific participating funds based on the weighted daily average share balance.

Treasury investment pools each have their own distinct investment strategies, goals, and holdings that reflect the differing needs of Commonwealth funds for income, cash flows, and investment risk tolerance. The USTIF investment pools are held within the CIP and BNY Mellon Bank. The short-term investment pools, also referred to as Pool 924 and Pool 999, comply with the investment policies as adopted by Treasury, and are highly liquid vehicles, which can consist of cash and short-term fixed income with a goal of providing a high degree of liquidity and security but only modest returns. Shares in this pool are classified as Temporary Investments. The Long-term Investment pool complies with the investment policies as adopted by USTIF, and is a less liquid vehicle, which allows for investment in assets that offer potentially higher returns with commensurate risk.

The USTIF investments as of June 30, 2017 and 2016 consist of \$11.8 million and \$13.6 million of Temporary Investments and \$236.5 million and \$208.8 million in Long-term Investments.

NOTE C - Receivables

A receivable is a legally enforceable claim for payment to a business or government by its customers or residents for either goods supplied and/or services rendered in execution of the customer's order or for government imposed non-exchange transactions for which payment has not yet been received.

Exchange transactions represent cash received for the aforementioned good or service delivery, investment sale proceeds, as well as interest on notes and loans. Non-exchange transactions include government imposed obligations such as taxes or other assessments.

Receivables on Investments Interest and Dividends are settlements effected as of the end of the reporting period for which related cash is expected to be received in the subsequent period. As of June 30, 2017 and 2016, the Investments Interest and Dividends Receivables totaled \$946.2 thousand and \$894.0 thousand.

Receivables on Investments Sold are related to sales of investments and anticipated payments associated with the sale of investments but which have not yet been received as of the statement date. As of June 30, 2017 and 2016, Receivables on Investments Sold totaled \$561.6 thousand and \$1.4 million.

Interest Receivable on Loan to General Fund is accrued interest calculated on the reported principal balance Advances to Other Funds. An advance (or loan) is a debt evidenced by a note which specifies, among other things, the principal amount, interest rate, and date of repayment. An advance entails the reallocation of the subject asset(s) for a period of time, between the lender and the borrower. The asset class Advances to Other Funds represents the balance of outstanding principal, net of allowance for loan loss, at the end the reporting period. As of June 30, 2017 and 2016, Receivables, Interest on Loans to the General Fund totaled \$15.1 million and \$14.6 million.

NOTE D - Advances to Other Funds

An advance represents resources that have been provided from one fund to another for repayment, in this case the General Fund. The asset or liability class represents the advanced fund resources that are expected to be received by the lending fund and repaid by the borrowing fund in the future. The advance was made to the General Fund on October 15, 2002 in the amount of \$100.0 million. To date \$32.5 million of the principal balance has been repaid with the most recent payment occurring in 2009. The original repayment in full date was to be June 30, 2014. This was amended during 2015 calling for \$7.0 million payments each October 15th until both the remaining principal and accrued interest are paid off in 2029. No payments have yet been made on the amended terms. Accrued interest, currently \$15.1 million, is determined monthly by applying the investment Pool 999 average monthly yield to the outstanding principal balance. As of June 30, 2017 and 2016, the Advances to Other Funds totaled \$67.5 million for each period.

NOTE E - Payables

A payable is money owed by a government or business to its employees, vendors, sellers of investments and/or grantees for which payment has not yet been rendered. *Accounts Payable and Accrued Liabilities* reflects vendor invoice disbursements that have posted through the end of the reporting period that have not cleared for payment from the State Treasurer, whereas *Invoices Payable* reflects invoice disbursements that have cleared for payment.

Accounts Payable and Accrued Liabilities as of June 30, 2017 and 2016, totaled \$15.3 million and \$15.6 million and Invoices Payable totaled \$2.2 million and \$1.9 million.

Investments Purchased Payable represents obligations of payment to sellers of investments associated with the routine operational investment activity of the fund. As of June 30, 2017 and 2016, the Investments Purchased Payable totaled \$1.2 million and \$3.1 million.

NOTE F - Due to Other Obligations

The liability class reflects resources payable to other Commonwealth or governmental funds for the reimbursement of goods or services provided or the enactment of a statutory transfer for which a cash transaction has not yet been effected. As of June 30, 2017 and 2016, the Due to Other Obligations totaled \$256.5 thousand and \$241.3 thousand. The following liabilities are included under Due to Other Obligations: Due to Other Funds; Due to Fiduciary Funds; Due to Other Governments and Due to Political Subdivisions.

Due to Other Funds

The inter fund cash transfer outstanding as of June 30, 2017 and 2016, of \$143.6 thousand and \$127.3 thousand are associated with a quarterly billing of the Insurance Liquidation Fund for consulting which is shared by the Worker's Compensation Security Fund and the Catastrophic Loss Benefit Continuation Fund.

Due to Other Governments

Due to Other Governments are obligations owed to the Federal government related to the payroll operations of the USTIF. These benefit obligations are attributable to Social Security and Medicare deductions from employees and related employer matching Social Security portions and are due to the Internal Revenue Service. As of June 30, 2017 and 2016, the Due to Other Governments totaled \$1.1 thousand and \$1.5 thousand.

Due to Fiduciary Funds

Due to Fiduciary Funds are obligations owed to other Commonwealth funds related to the payroll operations of the USTIF. These benefit obligations are attributable to retirement deductions from employees and are due to the State Employees Retirement System. As of June 30, 2017 and 2016, the Due to Fiduciary Funds totaled \$4.9 thousand and \$5.9 thousand.

Due to Political Subdivisions

Due to Political Subdivisions are obligations owed to other local governmental entities related to the operations of the USTIF. As of June 30, 2017 and 2016, Due to Political Subdivisions totaled \$106.9 thousand and \$106.6 thousand.

NOTE G – Other Liabilities

As all assets within a fiduciary agency fund are considered a custodial liability, no equity balances are reported. All residual funds are reflected as Other Liabilities.

As of June 30, the USTIF Other Liability balance is segregated and classified in the following manner:

Other Liabilities For:	2017	2016
Base for Environmental Cleanup	\$ 2,337,667	\$ 1,482,574
Catastrophic Release	25,253	20,798
Pollution Prevention	9,945	6,250
Investigation and Closure Costs	184,460	118,334
Other Encumbrances.....	1,513,203	1,055,627
Underground Storage Tank Indemnification	309,472,260	283,313,626
Total Other Liabilities.....	<u>\$ 313,542,788</u>	<u>\$ 285,997,209</u>

The following categories: Base for Environmental Cleanup program; Catastrophic Release program; Pollution Prevention program; and Investigation and Closure Cost program, reflect obligations of the Insurance Department relative to their respective cost categories.

The Other Encumbrances portion of the other liabilities reflects contracted obligations to vendors relative to administrative or operational activities of the fund. As of June 30, 2017 and 2016, Other Encumbrances totaled \$1.5 million and \$1.1 million.

The Underground Storage Tank Indemnification balance represents resources obligated to meet the known and unknown present and future claims liability and operations of the fund. As of June 30, 2017 and 2016, available balance for these disbursements totaled \$309.5 million and \$283.3 million.

NOTE H - Receipts and Disbursements

Receipts

Fees

The USTIF is financed by fees paid by underground storage tank owners or operators, distributors and tank installers. By law, the USTIF Board is required to evaluate the financial condition of the program annually. The agency's fee structure and collection methodology are described in regulations, which can be found at 25 Pa. Code 977.11 to 977.24. The current fees include:

Gallon Fees: Each distributor must assess a fee of \$0.011 per gallon on regulated substance deliveries to underground storage tanks (USTs) under agency regulation. The Gallon Fees for the fiscal years ended June 30, 2017 and 2016 totaled \$52.5 million and \$52.2 million.

Tank Capacity Fees: The owner or operator of USTs storing heating oil, diesel fuel, kerosene, and used motor oil products must pay an annual fee of \$0.0825 per gallon of tank capacity. The Tank Capacity Fees for the fiscal years ended June 30, 2017 and 2016 totaled \$6.2 million and \$5.9 million.

TIIP Fees: Tank Installer Indemnification Program (TIIP) is funded by two types of fees: a yearly company fee; and activity fees related to installations, removals, and major modifications of USTs performed by tank installers. In order to properly and accurately bill the company and activity fees, the USTIF depends upon data from the Department of Environmental Protection. The certified company must pay an annual activity fee of \$1,000. Additional activity fees of \$15 for tank removals and \$50 for installations or modifications are billed monthly. The TIIP Fees for the fiscal years ended June 30, 2017 and 2016 totaled \$327.4 thousand and \$299.2 thousand.

Investment Income

Investment income includes Interest and Dividend Income, Recapture of Broker Commissions, and Net Increase in Fair Value of Investments during the fiscal period. If the change in the fair value of investments decreases during any specific fiscal year, such decreases could cause reported overall investment income to be negative within specific funds. Similarly, realized losses could cause reported overall investment income to be negative within specific funds. For the fiscal years ended June 30, 2017 and 2016, Interest and Dividend Income totaled \$5.2 million and \$4.7 million; Recapture of Broker Commissions totaled \$4.7 thousand and \$18.8 thousand and Net Increase in Fair value of Investments totaled \$12.0 million and \$1.1 million.

Interest on Loans

Represents interest accrued on the outstanding balance \$67.5 million on the loan to the General Fund through the end of the year. Interest on Loans for the fiscal years ended June 30, 2017 and 2016 was \$543.9 thousand and \$234.5 thousand.

Other Receipts

Other Receipts include payments on charged off loans, cost recoveries and other miscellaneous items and for the fiscal years ended June 30, 2017 and 2016 totaled \$15.8 thousand and \$350.2 thousand.

Disbursements

Administrative

Administrative disbursements include Insurance Department Personnel, such as salaries, health and retirement benefits, Third Party Administrator fees and Professional Services. For the fiscal years ended June 30, 2017 and 2016, Administrative disbursements totaled \$6.7 million and \$5.8 million.

Claims Indemnification

Claims Indemnification disbursements mostly include losses on claims filed and the related legal and non-legal disbursements on those losses. For the fiscal years ended June 30, 2017 and 2016, Claims Indemnification disbursements totaled \$36.2 million and \$39.0 million.

Allocations - Funds Released

Allocations - Funds Released activities include disbursements for Environmental Cleanup Programs, Pollution Prevention Programs, Catastrophic Release Programs and Investigation and Closure Cost Programs. For the fiscal years ended June 30, 2017 and 2016, Allocations - Funds Released disbursements totaled \$6.0 million and \$6.5 million.

Supplemental Schedule

**Underground Storage Tank Indemnification Fund
Statement of Actuarial Claims Liability
(Unaudited)
As of June 30**

	2017	2016
Actuarial liability for estimated unpaid claims.....	\$ (382,700,628)	\$ (386,007,913)
Other Liability Balance for Underground Storage Tank Indemnification.....	309,472,260	283,313,626
Net Available (Unavailable) for Future Claims.....	<u>\$ (73,228,368)</u>	<u>\$ (102,694,287)</u>

The Statement of Actuarial Claims Liability provides a segregated presentation of the balances from the actuarial report associated with the Incurred But Not Reported (IBNR) claims and the other liability balance for Underground Storage Tank Indemnification available to meet these future claims payment obligations.

The USTIF, as an agency fund, provides claims payments to owners and operators of USTs who have incurred liability caused by leaks from USTs. The USTIF covers reasonable and necessary costs for corrective actions to clean up contamination from leaking tanks. It also covers claims for bodily injury and property damage that occur as a result of the release.

The Other Liability Balance for Underground Storage Tank Indemnification for future claims is \$309.5 million and \$283.3 million as of June 30, 2017 and 2016. Based on actuarial analysis as of June 30, 2016 (report issue date November 29, 2016), the estimated unpaid loss was \$382.7 million and \$386.0 million for June 30, 2017 and 2016.