

2/8/88

Statement of Need and Reasonableness

Institutional Energy Loan Program (IELP)

I. The Commissioner of the Minnesota Department of Public Service presents herein facts and justifications establishing the need and reasonableness of the proposed rules governing the Institutional Energy Loan Program. This program is funded with \$6 million of the \$36 million Exxon restitution allocation that the State of Minnesota received in 1986. Governor Perpich decided that \$6 million be dedicated to energy conservation loans for schools, hospitals and public buildings and that the Minnesota Department of Public Service administer the program. Distribution of these funds was contingent upon approval of this program by the U. S. Department of Energy. A state plan amendment to the State Energy Conservation Plan program outlining the intent for use of these funds was submitted to the U. S. Department of Energy and approved in June of 1987. These rules for the loan program are now being promulgated.

II. Impact on small business

The proposed rules create a voluntary program of financial assistance to Minnesota public and private non-profit schools, hospitals, nursing homes and units of local government to implement energy

conservation improvements and, as such, have no direct effect on small business. Rules covering programs such as this are exempted from Minnesota Statutes Section 14.115 (1986) by subd. 7(b) which exempts rules which do not directly affect small businesses.

III. Need and Reasonableness of each Rule Provision

A. Proposed part 7605.0010 states the purpose of the proposed rules. This part is needed to introduce the proposed rules and its reasonableness is self evident.

B. Definitions

Proposed part 7605.0020 defines terms which have distinct meanings when used within the context of these rules.

Subpart 1 is needed as an introductory and explanatory sentence regarding the use of the definitions. Its reasonableness is self evident.

Subpart 2 defines "applicant". Providing a shorthand term to reference those institutions eligible to borrow loan funds is needed and reasonable to make the rule more readable.

Subpart 3 defines "building". This definition is needed to identify those buildings which are eligible for the loan program. It is necessary and reasonable to specify existing because a conservation measure cannot be installed in a building not yet constructed. It is necessary to specify separate to make clear that when a building is referenced in rule, all parts of a building including wings and additions are implied.

It is reasonable to require that a building be owned and operated by a public or private-non-profit institution (as defined in this part) because, the Commissioner advised the U. S. DOE that loans would only be made to public and private-non-profit institutions. Approval by the U. S. DOE expenditure of these funds was made on that premise. It is also reasonable to require that a building be owned and operated by a private non-profit institution because the purpose of the loan program is to encourage such institutions to invest in energy saving capital improvements. While present ownership and operation does not guarantee that an institution will remain the beneficiary over the useful life of an improvement, if it is sold, such capital improvements should be reflected in the purchase price.

Subpart 4. Defines "commissioner". It is needed and reasonable to provide a shorthand term to make the rule more readable.

Subpart 5. defines "conservation measure". This definition is necessary to specify what kinds of projects are eligible. It is reasonable to limit projects to those eligible under the department's existing programs. This definition is consistent with the definition of conservation measure used in all of the department's other energy financing programs. Those capital improvement projects have a proven track record of energy savings.

Subpart 6. defines "financial institution". It is needed to specify who can make loans. It is reasonable to include a broad base of lenders to maximize use of program funds.

Subpart 7. defines "hospital". The Department of Public Service intends to broaden the definition in the final rule to match the definition of licenced hospitals as found in Minnesota Statutes Chapter 114.50.

Subpart 8. defines "lender" to mean the Minn. Department of Finance, a private or community foundation or a financial institution as defined in this part. It is reasonable to define lender to make clear what financing sources the Commissioner approve as lenders under the program. It is reasonable to include the Minnesota Department of Finance because a large

percentage of the money loaned under the program will be matched to loan funds distributed by the Department of Finance. It is reasonable to include private or community foundations because they often provide financial assistance to the institutions eligible for funds under this program. It is necessary and reasonable to limit the type of lenders because it will be the responsibility of the lender to conduct any credit analysis of loan applicants and to service the loan throughout the term of the loan.

Subpart 9. defines "nursing home." It is defined to insure that only licensed nursing homes can apply.

Subpart 10. defines "Payback". This definition is reasonable because it applies the most commonly used meaning, within the context of energy cost savings analysis, and is consistent with standard practice within the energy auditing field.

Subpart 11. defines "Private non-profit institutions". It is needed to clarify what private non-profit institutions can apply. It is reasonable because the U.S. DOE approved expenditure of these funds based on a plan that limited which private non-profit institutions are eligible for program funds.

Subpart 12. defines "Project". It is needed and reasonable to provide a shorthand term to make the rule more readable.

Subpart 13. defines "Public Institution". It is needed to clarify what public institutions are eligible for program funds. It is reasonable to limit eligibility to schools, hospitals, cities, counties and towns because the U. S. DOE approved expenditure of these funds based on a plan that limited the types of public institutions eligible for funds.

Subpart 14. defines "School" . It is needed to identify the types of schools eligible for program funds. It is reasonable to limit the type of school eligible to those eligible in other financing programs available in the department. It is reasonable to limit participation to public or private non-profit schools because these are the only institutions eligible to receive funds under this program.

C. Loan Eligibility Criteria

Subpart 1 establishes that the Commissioner approves IELP applications that comply with the rules for conservation measures that have a payback of ten years or less. It is necessary to specify Commissioner because he has the authority to approve or deny funds distributed under this program. It is reasonable to

limit the payback to ten years because the State funded Municipal Energy Loan Program and the Federal Institutional Conservation Program have ten year pay back limitations. It is reasonable that guidelines of this program be consistent with other financing programs administered by this department. A considerable portion of this program's funds will be used to match funds from the State's loan program. It is necessary to limit conservation measures to those with paybacks of ten years or less so that program dollars go to cost-effective projects that will ultimately save applicants money through energy savings.

Subpart 2 identifies eligibility limitations for projects. It is necessary because it prevents an applicant from receiving double funding for a project, while allowing funds to be used for cost over-runs or additional project related work, provided the project continues to meet program requirements. It is reasonable because it will prevent misuse of funds while allowing for loan amendments to cover unanticipated but reasonable costs.

Subpart 3 describes the prior approval condition of the program. A loan may not be awarded for a project already contracted for or begun. This is necessary to prevent a situation in which an applicant starts work on a conservation project anticipating funds from this program before having that project reviewed for technical feasibility and program compliance.

Subpart 4 is necessary and reasonable because it prevents funding measures that do not payback within the life of a building or energy using system. This limitation is reasonable because it is not economically wise to fund a project in a building that's useful life is less than the payback of the measure.

Subpart 5 addresses the ineligibility of new construction except as a necessary part of a conservation measure for an existing building or energy using system. Because the purpose of this program is to reduce energy consumption with the primary criteria being how quickly a conservation measure pays for itself, it is reasonable that only projects affecting existing buildings or energy using systems be eligible. It is reasonable to allow new construction where it is necessary for the successful implementation of a conservation project because it would be considered part of the project and so that the investment in new construction does not become a financial burden to the applicant.

D. Loan Limits

This part limits the use of program funds issued under this program not to exceed a maximum of 50% of the loan principal or \$200,000, whichever is less. The Department of Public Service staff and the program advisory committee concluded that the lesser of a 50% participation cap or a \$200,000 limit was

necessary to achieve the goal of spreading program funds to a large number of projects while still providing inducement to invest. With the 50% cap, a public school or local government would be able to decrease by one-half the interest rate currently offered under the state's Municipal Energy Loan Program. Private non-profit schools, hospitals and nursing homes could borrow at a rate of one-half that currently offered by banks.

E. Application Contents

Proposed part 7605.0050 describes the contents of a loan application and procedures for applicants to use in order to apply for a loan. Subpart 1 states that applicants shall submit an application to the Commissioner on a form provided by the Commissioner. This subpart is needed to provide a consistent format for all applications. This subpart also states that each application must have an original ink signature by an authorized official of the applicant, must have the authorized official's title and must be dated. It is necessary and reasonable to have this requirement to ensure that the responsible official is aware of the loan application and proposed projects, and he/she has, in a capacity as an authorized official, approved of the loan application.

Subpart 2 describes the contents of each loan application. The majority of the information required is needed to identify the applicant and contact individuals and to identify basic information about the proposed project or projects. It is necessary to require this information to determine eligibility and to maintain public records.

Subpart 3 describes the technical support materials that are required to be submitted with the application. The information required is necessary in order for DPS staff engineers to determine if the payback calculations that are submitted for projects are accurate and fall within program restrictions. This subpart requires that all conservation measures be analyzed using the energy conservation development sheet format available from the Commissioner. It is necessary to require this standard format so that eligible conservation measures are analyzed consistently for all applicants. It is reasonable to use the format available from the Commissioner because this format has been used for the past several years, and is the standard for many similar programs.

It is a necessary and reasonable requirement that for matching loans of \$25,000 or more, the technical analysis be conducted by a Minnesota registered mechanical engineer, electrical engineer, or architect. Although it would be desirable if all projects

funded under this program were analyzed by an engineer or architect, the expense of this level of expertise may be prohibitive for projects funded with matching loans of less than \$25,000. Because we want to encourage the greatest participation possible, funding both large and small scale energy conservation projects, it is reasonable to require the professional technical analysis only for loans for projects of \$50,000 or more.

It is necessary that applications include either the Engineering Analysis Report Summary or the Maxi-Audit Report Form so that necessary information is presented in a standard format which facilitates the requisite data processing.

Subpart 4 requires that applications contain a number of assurances. The first of these is that the applicant has provided for proper and efficient operation and maintenance of a proposed project. This requirement is necessary to protect the investment in an installation. This provision is especially important if special training or a new maintenance practice is required to operate or maintain a project. The second assurance requires that all work meet Minnesota building code requirements. This is necessary to meet federal State Energy Conservation Plan rules. The third assurance requires that the applicant identify the source of any funds required to pay for

portions of a project not eligible for program funds. This is necessary to assure that the entire project has financial backing before any construction begins or program funds are committed. The third requirement is that the applicant submit documentation that applicable voter approval requirements are met. This is necessary to insure that all applicable laws are obeyed. The fourth requirement is that an applicant document that it is able to accept and repay funds without exceeding applicable debt and levy limits. This is necessary to protect the state's interest in issuing loan funds. It insures that the loan itself is legal under the laws of the state.

Subpart 5 explains the procedure that will be followed if incomplete applications are submitted. The Commissioner will notify an applicant of specific deficiencies in an application so that the applicant has the opportunity to correct them and participate in the program. The 30 day limit on submitting corrections to an application is needed to prevent the administrative problem created by an unlimited number of pending applications, which remain unprocessable for an indefinite period of time. It is reasonable because 30 days is adequate time to correct deficiencies and because applicants retain the option of reapplying if they so choose.

Lender

This part specifies the contents of the agreement that must be executed between the lender and the Commissioner regarding conditions under which loans can be made and procedures that are to be followed in the event of default by the applicant. This agreement is necessary and reasonable to protect the loan fund's interest in the financial assistance.

Application Review

Subpart 1 outlines the administrative review of an application. It is needed to confirm that the items referred to are completed and will be checked by the Commissioner. It is reasonable because the Commissioner is responsible to see that these requirements are carried out.

Subpart 2 outlines the items that the Commissioner will review regarding technical analysis of the projects for which funds are requested. It is reasonable because it is the Commissioner's responsibility to check if the technical analysis upon which project feasibility is based is sound to assure that only projects that meet program guidelines receive funds.

Subpart 3 outlines the procedures for rejections and resubmissions. It is necessary that an applicant be notified of any modifications made to the application and all options available to correct problems with the application. The subpart explains that if only some of the measures are deemed acceptable by the Commissioner, the applicant may choose to accept a loan for those measures. This is reasonable if the rejected measures are not able to be modified for resubmission for technical or administrative reasons and allows the applicant to receive a loan without having to resubmit a new application. This could be critical if program funds ever become competitive.

Reports and Monitoring

Proposed part 7605.0080 describes the various reports required of loan recipients by the state. Subpart 1 is simply an introduction to the proposed part. The need and reasonableness of this introductory subpart is self-evident. Each of the four following subparts describes a different report.

Subpart 2, describes the annual project status report. This report is needed to assure the Commissioner that the loan funds are indeed being used for the purpose described in the application. It is easiest for the district to simply fill out a

supplied form rather than create a document more complex and detailed than needed. A short form annual report is a reasonable requirement, to balance the Commissioner's need for information on the project's progress, against the desirability of having a minimum number of reports for the loan recipient to complete. The time period July 1 through June 30 is needed to conform with the state fiscal year, and is reasonable because the reports come to a state office covering the use of state funds. The due date of July 31 is given to set a reasonable time limit on how long loan recipients may take to complete the report and send it in; a month is a reasonable period of time in which to expect completion and submission of a relatively simple form report.

The subpart describes the contents of the status report. This section is needed for two reasons: for the Commissioner to determine that the project is actually in progress and the loan funds are being properly used; and also for the Commissioner to have early notification of any loan recipients having difficulties with project implementation. Those having difficulties may be offered assistance in resolving the problems if the problems are known about soon enough. This provision is reasonable because the Commissioner must have some method of

verifying that funds are correctly used and because, if informed, the Commissioner may be able to offer assistance not only to the loan recipient involved, but may be able to solve in advance potential problems for future loan recipients.

The subpart continues by stating that if at any time the loan recipient fails to substantially comply with the start and end dates given in the approved loan application, and if the loan recipient cannot reasonably justify its lack of progress, the entire loan amount may become due and payable at the discretion of the Commissioner. This part is needed as a sanction to use in the event it becomes obvious that a loan recipient is not using the loan as agreed upon by both parties. It is reasonable because the part allows leeway for loan recipients that fail to comply with start and end dates for good reason. It is also reasonable not to require the Commissioner to call in all loans which cannot meet their estimated timelines, since there can exist justifiable reasons for deviation from timelines.

Subpart 3 describes the semi-annual financial report. These reports are needed to assure the Commissioner that funds are, in fact, being disbursed as work proceeds on the project. This is reasonable because it keeps the Commissioner informed of expenditures on a timely basis.

Subpart 4 describes the final report that must be submitted to the Commissioner within 60 days of project completion on forms

supplied by the Commissioner. This report is necessary and reasonable for the reasons described for the two preceding report. In addition, final reports are needed stating that the work is completed and provide data necessary to evaluate the program's effectiveness.

Subpart 5 covers the annual energy report. This report is needed to provide to the Commissioner actual energy data on which to evaluate the effectiveness of the program. It is a reasonable requirement because the goal of the program is to conserve energy and reduce energy costs for loan recipients. Annual energy reports provide data to assess whether that goal has been met and continues to be met. A minimum of three years of these reports is needed and reasonable to give a minimum amount of information with which to assess the impact of the project.

For the reasons stated above; the Department of Public Service believes that each of the proposed parts is reasonable to effectively administer the financial assistance program to distribute loans for the purpose of energy conservation retrofit in public and private non-profit schools, hospitals, nursing homes and city, county and town owned buildings. It is further believed that the proposed rules are reasonable and necessary to effect the purpose and intent of the statutory authorization.