



Department of Energy
Washington, DC 20585

SEP PROGRAM NOTICE 10-013
EFFECTIVE DATE: July 28, 2010

SUBJECT: GUIDANCE FOR STATE ENERGY PROGRAM GRANTEES ON QUALIFIED ENERGY CONSERVATION BONDS AND NEW CLEAN RENEWABLE ENERGY BONDS.

PURPOSE

To provide guidance to the Department of Energy's (Department or DOE) State Energy Program (SEP) grantees regarding Qualified Energy Conservation Bonds (QECBs) and New Clean Renewable Energy Bonds (New CREBs).

SCOPE

The provisions of this guidance apply to grantees of SEP funds, pursuant to Formula Grant or American Recovery and Reinvestment Act of 2009 (Recovery Act).

LEGAL AUTHORITY

SEP is authorized under the Energy Policy and Conservation Act, as amended (42 U.S.C. § 6321 et seq.) All grant awards made under this program shall comply with applicable law including the Recovery Act and other procedures applicable to this program.

GUIDANCE

Leveraging Funds under the SEP: Purpose and Type of Leveraging under SEP

Grantee arrangements for leveraging additional public and private sector funds, including rebates, grants, and other incentives, must be arranged to ensure that federal funds go to the "purchase and installation of energy efficiency and renewable energy measures." 42 U.S.C. § 6322(d)(5)(A). The leveraging of funds may be accomplished through supporting the issuance of QECBs and New CREBs, as discussed in this document.

Qualified Energy Conservation Bonds

SEP funds may be used to support the issuance of QECBs subject to the conditions identified in this section. QECBs are qualified tax credit bonds that may be used by state, local and tribal governments to finance qualified energy conservation projects. In order to ensure that a use of SEP funds for QECBs furthers the stated purposes of SEP, the projects supported by the QECBs must be for the purchase and installation of energy efficiency and renewable energy measures consistent with the SEP authorizing statute and regulations.

New Clean Renewable Energy Bonds

SEP funds may be used to support the issuance of New CREBs subject to the conditions identified in this section. New CREB are issued by public power utilities, electric cooperatives, government entities (states, cities, counties, territories, Indian tribal governments), and certain lenders to finance renewable energy projects.

In order to ensure that a use of SEP funds for New CREBs furthers the stated purposes of SEP, the projects supported by New CREBs must be for the purchase and installation of energy efficiency and renewable energy measures consistent with the SEP authorizing statute and regulations.

QECBs and New CREBs under the SEP

Grantees can use SEP funds toward supporting QECBs or New CREBs for the following purposes:

- (1) Debt Service Reserve Fund;
- (2) Capitalized Interest Fund; or
- (3) Principal Sinking Fund Payments

Debt Service Reserve Fund under the SEP

A debt service reserve fund (DSRF) is established by a qualified issuer of QECBs or New CREBs for payment of debt service on QECBs or New CREBs in the event pledged receipts are insufficient.

In order to ensure that a use of SEP funds to leverage additional public and private sector funds furthers the stated purposes of the SEP, the activities supported by the leveraged funds must be for the purchase and installation of energy efficiency and renewable energy measures consistent with the SEP regulations.

Capitalized Interest Fund under the SEP

A capitalized interest fund is established as a separate account by a qualified issuer of QECBs or New CREBs that pays interest on the QECBs or New CREBs for a specific period of time.

A grantee must ensure that the capitalized interest fund does not exceed the sum of the qualified issuer's net coupon payments that are due before the qualified project is complete and starts to generate revenue. The net coupon payment is the difference between the taxable coupon payment owed to the bond investor and the direct subsidy amount the qualified issuer receives from the Treasury. The direct subsidy is equal to the lesser of (i) 100% of the taxable interest payment owed to the bondholder or (ii) 70% of the applicable tax credit rate published daily by the Treasury.

Principal Sinking Fund Payments under the SEP

A qualified issuer of QECBs and New CREBs can deposit level payments on an annual basis in a principal sinking fund to be used for retiring bonds at maturity. Sinking funds can earn interest subject to arbitrage restrictions. The permitted sinking fund yield is fixed at pricing and limited to 110% of the long-term adjusted applicable federal rate, compounded semi-annually, reset monthly.

Additional Limitations on the use of SEP funds for QECBs and New CREBs

In addition to the limitations identified above, a grantee must ensure that the following conditions are met:

- a) a grantee shall have the right to review and monitor projects supported by QECBs/New CREBs to ensure that the projects are for the “purchase and installation of energy efficiency measures” as set forth in SEP authorizing statute and regulations;
- b) a grantee establishing a DSRF has no legal or financial obligation to commit additional SEP funds beyond the funds committed to the reserve;
- c) any SEP funds used to establish a DSRF not used in connection with debt service paid to bond holders must be used by or at the direction of the grantee and for an eligible use under the SEP;
- d) under no circumstances shall SEP funds be released to a bond holder for any purpose not pertaining to debt service; and
- e) DOE must complete National Environmental Policy Act (NEPA) review prior to the grantee issuing QECBs and New CREBS supported by SEP funds.¹ However, DOE has developed tools to expedite NEPA review in certain circumstances (e.g., the SEP NEPA Template, which facilitates DOE categorically excluding from further NEPA review entire QECB and New CREB programs if the programs are limited to certain types of projects). DOE encourages grantees to take advantage of these tools, which DOE identifies in its *SEP Program Notice 10-08, Guidance for State Energy Program Recipients on Financing Programs*. (See Guidance on page 4
http://www1.eere.energy.gov/wip/pdfs/sep_financing_program_guidance_10-08_revised_04202010.pdf)

¹ Nothing in this guidance addresses or affects the Department of Treasury’s NEPA obligations with respect to QECB and New CREBs.

As described below, a grantee is subject to certain limitations regarding the use of its SEP funds.

- a) Loan Loss Reserve Only, No QECBs or New CREBs are issued: pursuant to DOE's guidance entitled *SEP Program Notice 10-08, Guidance for State Energy Program Recipients on Financing Programs*. (See Guidance on page 4 http://www1.eere.energy.gov/wip/pdfs/sep_financing_program_guidance_10-08_revised_04202010.pdf), if a grantee chooses not to issue QECBs or New CREBs, it cannot use more than 50% of its SEP funds for loan loss reserves (LLR) to support a revolving loan fund;
- b) Loan Loss Reserve and QECBs or New CREBs are issued: if a grantee uses SEP funds for LLR to support a revolving loan fund and issues QECBs and/or New CREBs supported by a DSRF, capitalized interest fund and/or principal sinking fund payments, the total combined value of funds applied to these purposes cannot be more than 65% of the grantee's SEP funds, provided that the combined value of funds applied to an LLR and/or a DSRF cannot be more than 50% of SEP funds;
- c) Only QECBs or New CREBs are issued: if a grantee does not use SEP funds for LLR to support a revolving loan fund and issues QECBs or New CREBs supported by a DSRF, capitalized interest fund and/or principal sinking fund payments, the total combined value of funds applied to these purposes cannot be more than 65% of the grantee's SEP funds, provided that the value of funds applied to a DSRF cannot be more than 50% of SEP funds.

Obligation & Drawing Down of Funds

Debt Service Reserve Fund, Capitalized Interest Fund, and Principal Sinking Fund

Payments: Funds are considered obligated when they are committed to support QECBs or New CREBs under the SEP guidelines.

For DSRF, capitalized interest fund and principal sinking fund payments supporting QECBs or New CREBs, funds are considered obligated by sending a letter to the Project Officer indicating the establishment of the DSRF, capitalized interest account, and/or principal sinking fund payment account. Once funds have been obligated the funds may be drawn down from Treasury's Automated Standard Application for Payments (ASAP) system to fund the DSRF, capitalized interest account, and/or principal sinking fund payment account pursuant to DOE's guidance entitled *Guidance for SEP and EECBG Recipients on Payment Procedures* (see Guidance at http://www1.eere.energy.gov/wip/pdfs/eecbg_sep_asap_draw_down_guidance.pdf). ASAP is the system by which grantees receiving financial assistance from DOE can draw down the funds that have been pre-authorized by the agency for payment.

A DSRF, capitalized interest fund and principal sinking fund payments are considered expended after they have met the above requirements for obligation and the grantee has drawn funds down from the ASAP system to fund the account.

Program Income

All program income paid to grantees is subject to the terms and conditions of the original grant, including the provisions of 10 CFR § 600.225. Program income does not include interest on grant funds. *Id.* However, interest earned on advances shall promptly, but at least quarterly, be remitted to DOE. Grantees and subgrantees may keep interest amounts up to \$100 per year for administrative expenses.

Federal Requirements Applicable to Debt Service Reserve Funds, Capitalized Interest Funds, and Principal Sinking Fund Payments

NEPA, Davis Bacon Act (DBA), and the Buy American provision requirements apply similarly to debt service reserve funds as to other individual projects funded by Recovery Act awards, including capitalized interest funds and principal sinking fund payments under the SEP. There are steps that grantees can take to minimize delays associated with these requirements when the grantees seek to use Recovery Act-funded credit enhancement vehicles to support third-party financing of privately-funded projects.

The Department of Labor has stated in All Agency Memorandum 208 that the proceeds from QECBs and New CREBs are subject to DBA requirements and "all projects funded in whole or in part" from proceeds of these tax favored bonds are subject to the DBA. See <http://www.wdol.gov/aam/aam208.pdf>. Therefore, if an SEP grantee uses SEP funds to support the issuance of QECBs and New CREBs the proceeds from QECBs and New CREBs are subject to the DBA and all projects funded in whole or in part from proceeds of these tax favored bonds are subject to the DBA.



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