

STATE OF MINNESOTA
MINNESOTA ENERGY AGENCY

In the Matter of the Proposed
Adoption of Rules of the Minnesota
Energy Agency Governing the District
Heating Preliminary Planning Grants
Program, 6 MCAR §§ 2.4001-2.4007

STATEMENT
OF NEED AND
REASONABLENESS

INTRODUCTION

In its 1981 session, the Minnesota Legislature appropriated \$300,000 in fiscal year 1982 to the Minnesota Energy Agency ("Agency") for preliminary planning grants to be distributed to municipalities for planning related to the development of district heating systems. The Agency has developed these rules in accordance with Laws of Minnesota 1981, Chapter 356, Section 30 for the purpose of managing the distribution of the Preliminary Planning Grants.

The objective of the Preliminary Planning Grant Program is to encourage the development and expansion of economically viable district heating systems which have the potential to save energy or displace scarce fuels such as oil and natural gas. It is the intent of this program to encourage:

1. construction of new hot water district heating systems,
2. reconstruction or major expansion of existing steam district heating systems,
3. expansion of district heating systems by development of satellite systems or heat islands which could be connected to an existing or proposed central heating system.

This Statement of Need and Reasonableness will illustrate the manner in which the Agency, through the proposed rules, will provide state assistance to municipalities.

On July 6, 1981, a Notice of Intent to Solicit Outside Opinion concerning preliminary planning grant rules was published in the State Register at 6 S.R. 26-27. On August 10, 1981, a Notice of Intent to Solicit Outside Opinion Concerning Draft Rules Governing the Administration and Distribution of Preliminary Planning Grants for district heating systems was published in the State Register at 6 S.R. 174. This notice allowed for comments to be received until August 21, 1981. All comments which were received as a result of those notices have been considered, and where appropriate, incorporated in the promulgation of these rules.

RULES

The format used in preparing this Statement of Need and Reasonableness is as follows: each rule is stated and underlined; it is then followed by an explanation of the intent of the proposed rule and the need for the proposed rule.

6 MCAR § 2.4001 Authority and purpose.

A. Authority. Rules 6 MCAR §§ 2.4001-2.4007 implementing the district heating preliminary planning grants program are promulgated by the agency pursuant to Laws of 1981, ch. 356, § 30.

This section is necessary to indicate the statutory authority and requirement for promulgating these rules.

B. Purpose. The objective of the district heating preliminary planning grant program is to encourage the development and expansion of economically viable district heating systems which have the potential to save energy and displace scarce fuels such as oil and natural gas. The program shall encourage: construction of new hot water district heating systems; reconstruction or major expansion of

existing steam district heating systems; and expansion of district heating systems by development of satellite systems or heat islands which could be connected to an existing or proposed major central heating system later.

This section is necessary to indicate to interested parties the reason for the promulgation of these rules and the purpose of the program in which they may hope to participate. The language expresses the purpose of the program as discussed in the introduction to this Statement of Need and Reasonableness and as the Agency understands legislative intent regarding district heating.

6 MCAR § 2.4002 Definitions. For the purpose of 6 MCAR §§ 2.4001-2.4007 the words or terms defined in this rule have the meanings given them.

The Agency included in this rule definitions of terms used often in the rules which might not be understood by the reader and also terms which are used in a shorthand manner in the rules.

A. Agency. "Agency" means the Minnesota Energy Agency.

The term Agency means the Minnesota Energy Agency as provided in Minnesota Statutes sections 116H.01 to 116H.15. This definition is necessary in order to identify the state agency charged with the responsibility of promulgating rules for this program and administering state assistance. It is used often in the rules.

B. Applicant. "Applicant" means a municipality as defined in F as well as any organization submitting a joint application with the municipality. No application shall be accepted unless submitted by a municipality as sponsor or co-sponsor.

This definition acknowledges that entities other than the municipalities applying for grants may be the driving force behind a district heating project.

C. Community Heatload Survey and Map. "Community heatload survey and map" means a description of the district heating market including location of heat source, location, type and age of heating systems of potential nonresidential customers, annual energy consumption and temperature requirements and approximate load duration for process heat customers.

The legislation requires that applicants provide this survey and map and so its contents are specified here. The required contents include information essential to determining the likelihood of a projects success.

D. Director. "Director" means the director of the Minnesota Energy Agency.

This definition is necessary to identify the person responsible for receiving, reviewing, ranking and submitting recommended applications to the legislative advisory committee. It is also necessary for a grant recipient to know who will be responsible for evaluating monthly and final reports.

E. Major Central System. "Major central system" is one that does not rely on oil or natural gas.

An objective of the program is to encourage district heating projects that save oil and natural gas by using coal or waste heat. However, it is often more practical to develop a new district heating system using temporary heat sources, e.g., oil and natural gas, and later, when the market is larger, to convert to lower cost and more readily available energy sources. Major central system is defined based on energy source to distinguish it from new smaller systems, or satellite systems that have the potential to be converted from precious oil and natural gas to coal and waste heat.

F. Municipality. For purposes of applying for grants under this program, "municipality" means a city however organized.

This definition is necessary because the enabling legislation limits applicants to municipalities and does not define municipalities. Therefore, the Agency has taken the definition from Minnesota Statutes, section 414.011.

G. Project. "Project" means the preliminary planning project.

This definition is necessary to distinguish between preliminary planning project and later stages of developing a district heating system.

H. Satellite or Heat Island. A "satellite or heat island" system relies on oil, natural gas or the combustion of waste material and is a heating system which in the future would become a part of a major central system.

An important way of expanding district heating is to establish small satellite systems that can be developed to a size which warrants connection to the central system. Because it is important to encourage expansion of district heating, satellite systems are included in the program.

6 MCAR § 2.4003 Preliminary planning grant program.

A. Application schedule. The agency shall accept grant applications on two-month intervals after the effective date of 6 MCAR §§ 2.4001-2.4007. Applications received shall be ranked, and the director shall recommend ranked applications which meet all the criteria to the legislative advisory committee for approval and funding. No municipality shall be awarded more than two grants out of the same appropriation.

A two-month interval is both needed and reasonable since the Agency must have time to read and evaluate all applications. This 60-day period will also give the Agency a chance to administer one set of grant agreements as required in 6 MCAR § 2.4006 before beginning another set, which will help the process run smoothly. Several funding sequences are reasonable because communities are given an

opportunity to learn from each other which will help to improve the quality of the applications. Also, if quality of applications is improved, the public money will be used more effectively.

Each application will be ranked by the Agency according to the criteria stated in 6 MCAR § 2.4005. Each application containing all the information described in 6 MCAR § 2.4004 will be ranked and submitted to the legislative advisory committee for approval and funding. Applications not containing at least the minimum information will not be submitted to the legislative advisory committee and will instead be returned to the applicant.

It is reasonable not to fund more than two applications from the same municipality out of the same appropriation. This is needed to make certain every community has a fair chance.

B. Review Process. Applications shall be reviewed and ranked by the agency. The director shall prepare and submit to the legislative advisory committee a list of all district heating grant requests. The list shall contain the necessary supporting information. The recommendations of the legislative advisory committee shall be transmitted to the Governor. The Governor shall approve, disapprove, or return for further consideration each project recommended for approval by the legislative advisory committee. Upon approval by the Governor, a grant agreement shall be negotiated with the agency in accordance with 6 MCAR § 2.4006. Comments on applications not selected for grant awards will be forwarded to the applicant. Applications not funded shall be included in the next funding round unless withdrawn. Applicants may modify or supplement their proposal for the next funding interval if desired.

6 MCAR § 2.4003 B is needed to inform the applicant of the channels each application must go through. This review process is mandated by Laws of 1981, ch. 356, § 30.

The review process is reasonable because those communities that have deficiencies in their applications are not automatically rejected. In accordance with 2.4003 A., the two-month interval

gives the Agency a chance to comment on proposals not selected and gives the communities a chance to modify their proposals for a subsequent funding round.

6 MCAR § 2.4004 Contents of preliminary planning grant applications. Applications shall contain the information required by Laws of 1981, ch. 356, § 30, and at least the following information:

Since municipalities who desire preliminary planning grants must request them, it is necessary and reasonable that the Agency specify what must be included in the application for the Agency to properly assess the request. Certain of the required information is expressly required by the enabling legislation. The reasonableness and necessity of the individual data requirements are discussed below.

A. A community heatload survey and map. The survey shall contain a description of the heat source and an estimate of the district heating market.

1. If plans call for an existing heat source such as an electric generation plant or a coal-fired boiler, the application shall include at least a discussion of: type, size, age, fuel, present use and emission controls. If a new heat source is proposed to be used, the application shall include: fuel, estimated cost of fuel and fuel availability.

2. The estimate of the district heating market shall contain nonresidential building information including location, type and age of heating system, type of fuel and annual energy consumption and a description of process load including temperature requirements and load duration.

3. The map shall show the location of the heat source and major load concentrations.

The information contained in the community heat load survey is necessary to determine if a district heating opportunity exists in a community. The information required will be useful to the Agency in evaluating and ranking proposals.

Economic district heating systems require the thermal energy users to be relatively close to the heat source. The map is necessary to illustrate the proximity of users to the heat source as well as the density of the potential users.

B. Community benefit. Briefly discuss the impact of the district heating system on the community and how it would relate to community development plans.

C. Community commitment. Include written expressions of interest and commitment from major potential loads, owner of heat source, and the municipal governing body.

Community benefit and community commitment. Applicants that can demonstrate a community benefit are more likely to succeed in developing a district heating system. Development of a district heating system requires commitment and participation from all segments of a community. If there is substantial community benefit, the chances of obtaining this commitment are greater. It is reasonable to require that the commitment and benefit be demonstrated.

D. Project plan. The project plan shall include a list of tasks, time estimates for each task and a list of deliverables. It should also include rough estimates of time required in successive stages such as design and construction.

Applicants should demonstrate that their plans can effectively carry out the preliminary assessment. By requiring an applicant to include a preliminary estimate of the time it will take to develop a district heating system to construction, the applicants' awareness of the fact that this is normally a long and complicated process will be intensified.

E. Project budget. Include an estimate of expenditures by category, e.g. personnel, travel, etc., also estimates of costs by project plan task.

The budget is necessary to show the Agency how the grant money will be spent.

F. Project organization chart and use of consultants. Assistance in preparing applications can be obtained from the Agency.

It is necessary to know the type of consultant (engineering vs. economic) and who will be actually performing the work. The

Agency will be using its experience in previous projects to assist the communities in their preliminary assessments. The organization chart is the first piece of information needed to begin helping them.

6 MCAR § 2.4005 Ranking criteria. Applications will be ranked according to the following criteria, which are listed in order of importance:

The criteria of 6 MCAR 2.4005 are needed so the applicants know the standards by which their application will be judged. A ranking system is necessary since the number of grants allowed by current appropriation is limited and it is, therefore, important that the planning projects which have the highest probability of proceeding to construction are funded.

Anything which will support the granting of an application even though not clearly required by any of the rules or criteria should be included in the application. The Agency has not stated the criteria in greater detail because applicants may limit information provided to the Agency. Applicants should provide any information which will better sell their project.

A. Estimated capital cost per million BTU of energy sold per year.

Heat from district heating systems will be used only if it is economically competitive in the long run with other heat sources. In applying criteria, this formula will give the Agency an indication of the competitiveness of the proposed system which relates to the chances of it being successfully developed. This is the highest ranked criteria because if district heating is not economically competitive in the long run the other factors are irrelevant.

B. Benefit to the community.

Since these grants are made with public money, the Agency feels it is important that the general community benefit. The applicant should be aware that the Agency will look at this factor in its ranking. Examples of community benefit might be environmental benefit, significance for jobs, significance to community in low cost energy, development of an industrial park, coincides with long and short range planning, and others.

C. Project plan.

Completeness and credibility of project plan will be important factors the Agency will consider in determining whether state funds will be used efficiently and effectively.

D. Community commitment.

It is the Agency's experience that systems which have very little community involvement do not succeed. Therefore, a demonstration of community commitment at the outset will be required.

E. Thoroughness of community heatload survey.

Although the heatload survey and map are the first item mentioned in the legislation, they are listed here below economic competitiveness, community benefit and commitment because it is the totality of the rules and not the survey and map by themselves that are important. The survey and map are used as a ranking criteria to show the applicant that reliable information is expected.

F. Qualifications of project personnel.

This is listed as a criterion to assure that it is included in the application. It is doubtful that applicants will be graded down on their selection of a consultant.

G. Clarity and conciseness.

It is important that an application is clear and concise and is understandable to Agency personnel. The Agency does not elevate form over substance and glossy applications are not expected.

6 MCAR § 2.4006 Agreement. After approval by the Governor, the applicant shall enter into an agreement with the agency.

It is necessary and reasonable for the Agency to require individual agreements with each grantee to appropriately deal with the great variations in the projects to be proposed. 6 MCAR § 2.4006 is needed in order to inform the prospective grantee that a contract will be drawn up between the successful applicant and the Agency for purposes of formalizing the duties, activities, and obligations of the grantee and the Agency.

A. The agreement shall specify the grant amount and the duration of the grant. The agreement shall include assurance that the local share will be provided and that the agreed-upon work program will be carried out. A grant agreement based upon a joint application must be executed by the lead applicant. Amendments and extensions may only be made in writing and must be signed by all parties.

It is reasonable and needed that the contract specify the amount of the grant and the period of time the grant will cover. This will also aid the municipality in predicting the cash receipts relative to the expenditure of funds. The provision for assurances that the local share is being provided is both needed and reasonable in order to assure the Agency that the local unit of government is making a significant contribution while at the same time being the recipient of some of the financial and technical resources available from the Agency.

The requirement of the lead applicant, of a joint application, executing the contract is reasonable and needed in order to designate who will be in charge of administering the grant on the local level and formalizing that relationship between the lead applicant and Agency.

It is also needed and reasonable for the Agency to allow for contract amendments because of problems or situations which may necessitate program change. At the same time it is needed and reasonable that these amendments be made in writing and approved by the grantee and the Agency so that both parties remain aware of their responsibilities and obligations under this program. The need for justifying any grant extension in writing is reasonable to the grantee and the Agency because it will supply the opportunity to supply suggestions which may be helpful in resolving any problems which may be inhibiting successful completion of the agreed-upon tasks.

B. Funding period. Planning grants will be approved for a period of up to one year.

6 MCAR § 2.4006 B. is needed to inform the municipality that a period of up to one year will be allowed for the completion of a planning grant.

Most planning agreements will be written for a period of not more than six months, however, the Agency wants the flexibility of being able to extend this up to one year to accommodate schedules for other city projects that might impact the district heating plan.

6 MCAR § 2.4006 B. is reasonable because it provides sufficient flexibility to implement a project based on the scope of work

predetermined by the Agency and the grantee. This flexibility is necessary because the kinds of projects funded under this grant program are extremely diverse and will require varying amounts of time to successfully complete.

C. Grant limitations.

1. Planning grants shall not exceed 90% of eligible planning costs.

2. No single grant shall exceed \$20,000.

Rule 6 MCAR § 2.4006 C 1. is needed to clearly state to the applicant that a planning grant shall not exceed 90% of the total eligible planning cost for their district heating planning project. This 10% local cash match ratio is reasonable because it shows a significant local match which when combined with the Agency's grant amount can be used to help solve the local energy problems.

6 MCAR § 2.4006 C 2. allows for the Agency to grant planning monies up to 90% on a projects total cost, not to exceed \$20,000. These maximums of 90% and \$20,000 are specifically prescribed in Laws of 1981, ch. 356, § 30.

Furthermore, if the Agency is willing to contribute up to \$20,000 the local unit of government should be willing to contribute at least 10% because it will be the primary recipient of the benefits that are derived from the project.

D. Disbursement schedule. Ninety percent of grant monies shall be disbursed at the outset upon receipt of invoice to the agency of project costs. The remaining ten percent shall be disbursed upon completion and receipt of a satisfactory final report.

This rule is needed for the applicant to understand on what basis or schedule grant funds will be made available to the applicant.

The provision of 90% of the grant funds during the first month of the contract period is reasonable because of the sudden increase in expenses directly associated with the grant program and the short (2-6 month) time frame. These sudden costs are for expenses such as salaries, fringe benefits, materials and supplies, and contractor expenses.

It is also reasonable for the Agency to withhold 10% of the grant amount until a satisfactory evaluation has been completed. This is needed and reasonable in order for the Agency to be sure that the grantee has completed all of the agreed-upon work program and that the local unit has contributed its local share.

E. Required reports. The grantee shall submit to the agency on the first of each month a report briefly stating the activities that have transpired during the month. The grantee shall provide the agency with three copies, one of which shall be a camera-ready copy, of the final preliminary planning report.

This rule is needed to inform the grantee that brief monthly reports to the Agency will be required to keep the Agency informed on the progress of this recipient's program. This is a reasonable requirement placed upon the grantee that will inform the Agency of the program's status and provide an indication of when and how the Agency may be of assistance to a community in bringing about the successful completion of its planning program.

It is also reasonable for the grantee to provide the Agency with three copies including a camera-ready copy of any final reports developed for the community under this program. The provision of three copies will allow the Agency to keep copies readily available

and allow for copies to be easily reproduced which will help to make the information contained therein more accessible to other communities or agencies in the State of Minnesota. State law limits the number of copies that may be required to three.

F. Records. The grantee shall maintain for a period of not less than three years from the date of the execution of the contract all records relating to the receipt and expenditures of grant monies.

This requirement is needed and reasonable in order to comply with Minn. Stat. § 138.17 and the Agency's record retention schedule which was prepared pursuant to this law.

G. Contract deviations. No grant funds shall be used to finance activities by consultants or local staff if the activities are not included in the grant contract, unless agreed upon in writing by the agency. Unless agreed upon by the agency, a municipality may not contract out all its energy-related activities to consultants.

This is both needed and reasonable because it informs the grant recipient that it is bound by the grant contract to fulfill the requirements of that contract. It also indicates to the possible grant recipient that the final grant application and contract should accurately reflect the concerns addressed. Likewise it indicates that the local staff can reasonably and usefully work on the project. Any deviations to the contract must be made in writing in order to assure the Agency that the activities and expenses are allowable under this programs rules.

It is also reasonable not to allow 100% of all activities to be done by consultants. If the Agency were to allow 100% grant expenditures for consultants it is likely that the local unit of government will not be deeply involved in the planning process.

By not allowing all grant expenditures to consultants the local unit will be more responsible for portions of the district heating development plans. This in turn will increase the likelihood that the plan or portions of that plan will be implemented.

6 MCAR § 2.4007 Evaluation.

A. The Agency shall conduct an evaluation within 60 days of the submission by the Grantee to the Agency of the final report and all the required reports and financial documents. The evaluation shall assess:

1. Whether the local share contributed was equal to or greater than 10% of the total cost of the preliminary planning project.

This evaluation requirement is necessary and reasonable to evaluate the program to see if the program ratios are met.

2. Whether the agreed-upon work program was completed.

This is necessary and reasonable in order to see that the local unit has fulfilled its obligation as detailed in the grant contract. This portion of the evaluation will be based on the final approved application and the signed contract agreement.

3. Whether the governing body has formally reviewed the completed preliminary district heating plan.

This requirement is necessary to insure that the governing body which submitted the application has formally reviewed the documents which are developed from the work of this program. This is intended to insure that the governing body of the local unit formally considers the findings of the program and considers for implementation the aspects of the program which may assist in the resolution of the local unit of government's energy problems.

B. Upon completion of a satisfactory evaluation the remaining 10% of the grant shall be disbursed to the grant recipient. If the results of the evaluation are unfavorable to the grantee and

the grantee does not agree with the findings of the evaluation, the grantee may request a review by the director.

It is also reasonable that the state will then provide the remaining 10% of the grant contract amount. It is necessary for the state to withhold the last 10% of grant funds in the event that the agreed-upon work program is not completed. Because the Agency is investing heavily in the future, the director must have some recourse, such as withholding 10% of the grant funds, if contract obligations are not fulfilled.

It is also needed and reasonable to allow the grantee a review before the Agency in the event that an evaluation is unfavorable to the grantee. This hearing will provide an opportunity for the grantee to submit information or evidence to the director upon which the director can reconsider the decision that performance did not meet the standards set.

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MINNESOTA ENERGY AGENCY
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By

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