

State Water Infrastructure Authority
September 19, 2023 Meeting
Agenda Item M – Priority Rating Systems for Construction Project Revisions Related to the
Viable Utilities Reserve

Division of Water Infrastructure Staff Report

Background

The Viable Utility Committee (VUC) of the State Water Infrastructure Authority (Authority) met most recently on August 15, 2023 to further discuss two items related to the Division of Water Infrastructure’s (Division) Viable Utility (VU) program:

- Priority Rating Systems for Construction Projects Revisions Related to the Viable Utilities Reserve (Note: This is an Action Item)
- Review of Identification and Assessment Criteria Used in the Local Government Unit (LGU) Reassessment Process

This staff report focuses on the first item. The second item will be addressed briefly during the Authority meeting but is not directly addressed in this staff report.

History

General Statute 159G-35(c) directs the Authority and Local Government Commission (LGC) to develop evaluation criteria for grants from the Viable Utility Reserve (VUR), among other responsibilities. The Authority has decided to use the existing Priority Rating Systems (PRS) to prioritize awards made from various funding programs, including the State Revolving Funds (SRF), State Reserve Program (SRP) and (with some PRS modifications) the Community Development Block Grant – Infrastructure (CDBG-I) program. The Authority has also opted to use the PRS to prioritize awards to distressed (LGUs), including awards made from the VUR.

Following the Authority’s awards from the Spring 2022 funding round, the Chair of the LGC, State Treasurer Dale R. Folwell, sent a letter on September 7, 2022 to the Authority requesting that the Authority consider prioritizing funding for construction projects for LGUs under the financial control of the LGC per their authority under G.S. 159-181(c). The Authority and the Viable Utility Committee (VUC) discussed this request at prior meetings.

Local government units under the financial control of the LGC are automatically designated distressed under Identification Criterion 1 of the Identification Criteria adopted by the Authority and the LGC (so-called “D1 units”):

A unit whose fiscal affairs are under the control of the Commission pursuant to its authority granted by G.S. 159-181 (“under Commission fiscal control”)

Discussion

The Division of Water Infrastructure (Division) and Authority recognize that addressing the needs of D1 units can be challenging for several reasons:

- These LGUs are among the most distressed in the state, and paths to viability are often complex and require significant advanced planning to implement.
- Local government unit management of D1 water and wastewater systems is typically insufficient, and decision-making becomes the responsibility of the LGC and its staff.
- The LGC and its staff typically have neither the background nor the available financial resources to effectively manage the water and wastewater systems for D1 LGUs, thus requiring an inordinate amount of staff effort, coupled with emergency operating grants (EOGs), to continue providing services to customers.
- D1 construction project funding applications may or may not score well under the Authority's existing PRS, depending on the specific attributes of the LGU and its application.

This issue has been discussed during several VUC and Authority meetings. Authority members expressed a desire to continue to operate consistently with the existing PRS for VUR-funded construction projects, which is the same as that used for prioritizing projects for the SRFs and SRP. Because distressed LGUs are eligible for other funding programs in addition to the VUR, and because the Division typically tries to provide “the best” funding for the project, there is an efficiency for both applicants and application reviewers to use a common PRS.

Accordingly, the Division has implemented efforts short of formally revising the PRS to better facilitate D1 unit viability and support Commission staff. These include:

- PRS *guidance* changes that better reflect VU programmatic requirements to incentivize functionally equivalent options for priority points and further prioritize distressed LGUs making progress on statutory requirements and/or projects promoting viability (note that these ideas were discussed during the January 2023 VUC meeting).
- Suggested legislative change to G.S. 159G to relax funding caps and time limits on EOGs (which are only available to the LGC for D1 LGUs).
- Convening monthly planning meetings between DWI and DST to coordinate activities regarding D1 LGUs, including providing technical support to DST staff as needed.
- Offering application preparation assistance (complimentary reviews of draft applications to ensure that all available points are adequately justified) to all distressed LGUs.

Additionally, Division staff and the VUC recognize that the Authority has the discretion to prioritize funding recommendations based on additional information in the application that may not affect the application score. In other words, the Authority may prioritize funding awards in an order that differs from that based on the application score alone.¹

The VUC considered several staff recommendations during their August 15, 2023 meeting. The recommendations fell into three main categories:

1. Eligibility requirements for VUR funding
2. Application modifications that provide additional project context or details for Authority consideration for making funding awards
3. PRS modifications to further prioritize D1 LGUs
4. Allowing for more favorable funding terms (i.e., more grants/PF instead of loans) for D1 LGUs

Staff/Committee Recommendations

Based on discussion with the VUC, the Division intends to implement the following application preparation guidance and review modifications:

1. Require all distressed LGU applicants to have completed and be in good standing with the required initial Viable Utility education and training (i.e., Best Utility Management Practices [BUMP] training) to be eligible for VUR grant funding.
2. Require that, if the LGU has developed an Action Plan, the application must be consistent with the Plan's associated project priority list. If the LGU does not have an approved Action Plan, the applicant must provide an explanation addressing the LGU's progress in developing an Action Plan as required by distressed units under 159G-45.
3. Require distressed LGU applicants to submit a supplemental narrative in the application explaining how the proposed project is eligible under NCGS 159G-32(d) and how the proposed project will move the unit toward viability or address the issues that contributed to their designation.
4. Allow D1 LGUs to qualify for up to 100 percent principal forgiveness under SRF programs and up to 100% grant eligibility for the SRP.
5. Allow additional PRS points for D1 LGUs, by:
 - a. Allowing D1 LGUs to be eligible for 2.B.1 or 2.C.1 points in the construction PRS if the project will specifically address infrastructure, organizational and financial issues that have made them distressed. This will require a pre-

¹ By federal law, drinking water projects funded from the Drinking Water State Reserve Fund must be funded in priority order, so the bypass option is not available for this program.

application meeting between Division and LGC staff to discuss the eligibility of proposed projects for 2.B.1 or 2.C.1 points.

- b. Allowing applicants to claim the maximum number of Affordability (Category 4) points (i.e., 25) if the LGU has been awarded EOGs, which are only available to the LGC for D1 LGUs, within either the current or previous fiscal year.

Action Item

Based on discussion with the VUC and consistent with motions approved by the VUC, Division staff recommend that the Authority:

- Allow additional PRS points for D1 LGUs, by:
 - a. Allowing D1 LGUs to be eligible for 2.B.1 or 2.C.1 points in the construction PRS if the project will specifically address infrastructure, organizational and financial issues that have made them distressed. This will require a pre-application meeting between Division and LGC staff to discuss the eligibility of proposed projects for 2.B.1 or 2.C.1 points.
 - b. Allowing applicants to claim the maximum number of Affordability (Category 4) points (i.e., 25) if the LGU has been awarded EOGs, which are only available to the LGC for D1 LGUs, within either the current or previous fiscal year.

ADDENDUM: Supplemental VU Program Information (from August 15, 2023 VUC meeting staff report)

From a bigger picture perspective, the Division is considering moving toward a “programmatic funding” framework for VUR funding. Under such a framework, the Action Plans required of distressed LGUs under NC GS 159G will typically include an LGU-specific “project priority list”, developed by consensus between the LGU and the Division, along with a funding plan, including (but not necessarily limited to) the eligible funding available from the VUR (i.e., \$15M per unit, and up to \$30M for mergers). This framework could also allow the Division and Authority to prioritize among the group of distressed LGUs, so that LGUs with the most acute problems could preferentially receive funding.

However, such a framework relies on having stable, recurring funding. To date, outside of funds from the American Rescue Plan Act, the VUR has only received non-recurring funding at the discretion of the General Assembly.

Nevertheless, the VU program was designed by the legislature to require asset inventory and assessment and the development of short- and long-term action plans that would be used to direct capital project funding or funding for other efforts to improve LGU viability (e.g., paying off historical debt). The current structure of the VUR funding and prioritization process does not always facilitate these “other efforts” as some of the actions may not score well under the approved PRS.

The Division intends to move towards a programmatic funding framework for the VUR, which would:

- Depend on having a relatively consistent and reliable amount of VUR grant funding for at least a 10-year period (requires legislative action).
- Establish funding plans as part of the long-term plan and financial plan required of distressed LGUs. Approved funding plans from distressed LGUs could then be compiled by the Division, prioritized internally and with the Authority and LGC, and programmed out over a Departmental planning horizon (again, 10-year minimum is suggested). This would ensure that projects funded by the VUR derive from approved Action Plans, and that projects best reflecting state (e.g., Authority and LGC) priorities are preferentially funded.