

Meeting Summary

Clean Water State Revolving Fund Rulemaking Advisory Committee, Meeting 2

Wednesday, Feb. 26, 2020
DEQ Headquarters
700 NE Multnomah St.
Portland, Oregon, 97232



State of Oregon
Department of
Environmental
Quality

List of Clean Water State Revolving Fund 2020 Rulemaking Advisory Committee Member Attendance (in person or by phone)

- Quinn Andreas, Rural Community Assistance Corp.
- Chris Baily, Operations Manager, City of Albany representing League of Oregon Cities
- Charlotte Bentley, Community Program Director, USDA Rural Development
- Tom Elliot, Building Energy Analyst, Oregon Department of Energy
- Janna Graham, Public Finance Officer, Business Oregon
- Karen Lewotsky, Rural Partnerships Director, Oregon Environmental Council
- Eann Raines, Conservation Investments Coordinator, Clackamas Soil & Water Conservation District
- Desiree Sideroff, Consumer Lending Director, Craft3
- April Snell, Executive Director, Oregon Water Resources Congress
- Chris Thomas, Staff Attorney and Policy Specialist, The Freshwater Trust
- Doug Waugh, Finance and Administrative Services Manager, Clackamas Water Environment Services representing Oregon Association of Clean Water Utilities
- Absent: Sarah Absher, Planning Director, Tillamook County representing Association of Oregon Counties

Clean Water State Revolving Fund

700 NE Multnomah St.,
Suite 600
Portland, OR 97232
Phone: 503-229-5622
800-452-4011
Fax: 503-229-6124
Contact: LeeAnn Lawrence

www.oregon.gov/DEQ

*DEQ is a leader in
restoring, maintaining and
enhancing the quality of
Oregon's air, land and
water.*

DEQ staff attendees (for all or part of the meeting)

Lynn Barlow (CWSRF Program Manager), Dave Belyea (Regional Environmental Solutions), Kathy Estes (CWSRF Senior Loan Specialist), Justin Green (Water Quality Administrator), Rian Hooff (Sr. Policy & Legislative Analyst), Jennifer Kenny (CWSRF Program Analyst), Rebecca Kramer (CWSRF Project Officer), Lee Ann Lawrence (CWSRF Program Coordinator, Rulemaking Lead), Chris Marko (CWSRF Program Analyst), and Oscar Orejel (CWSRF Loan Specialist)

Members of the public

Pat Lando (Recode), Ashley Watkins (Yamhill County)

Facilitation Team

Colby Mills and Donna Silverberg, DS Consulting

Handouts and presentation materials

- [Agenda](#)
- [PowerPoint Presentation: Septic Systems Issues & DEQ Program in Oregon](#)
- [PowerPoint Presentation: CDFI Lending](#)

Introductions and Purpose

Donna Silverberg, facilitator from DS Consulting, welcomed everyone to the meeting. She reminded the group that the purpose of the initial meeting in January was to ground the committee in DEQ's current program and introduce Community Development Financial Institutions. This second meeting was a processing phase for DEQ and the Rulemaking Advisory Committee to clarify outstanding questions and to further explain the legislative intent behind Senate Bill 884, DEQ's onsite septic system program and related septic system issues in Oregon, and CDFI lending practices and issues. She clarified that DEQ is responsible for producing the final rules for the implementation of pass-through lending to CDFIs, as stated in SB 884, with consideration to the advice and recommendations provided by the RAC.

Review Legislative Intent: Clean Water Loans and Senate Bill 884

DEQ Senior Policy and Legislative Analyst, Rian Hooff, reviewed the legislative intent behind SB 884, and how a RAC was formed to advise on future administrative rules and properly evaluate the proposed lending program. In the 2016 legislative session, lawmakers addressed growing concerns about failing septic systems and their implications for environmental and public health, specifically through nonpoint source water pollution. To address this, they allocated \$250,000 of state general fund money to Oregon DEQ to establish a septic system (onsite) loan program, particularly for low-income Oregonians, especially, small businesses and residents, without access to traditional loan options.

DEQ used an open process for a Request for Grant Proposals from organizations to administer and issue loans for septic system repair and replacement. DEQ received one response, from Craft3, which is a certified CDFI. DEQ issued general funds to Craft3 through a grant agreement which has been amended four times to extend additional funding or time. DEQ manages the grant and works closely with Craft3 on reporting and invoicing for fund dispersal. This became the Clean Water Loans program in DEQ.

In 2019, the legislature passed SB 884 with the intent of narrowly expanding the definition of eligible borrowers for DEQ's Clean Water State Revolving Fund to include CDFIs. The bill made clear that these loans would be specifically for the purposes of replacing or repairing failing septic systems or connecting to municipal sewer lines. The bill amended Oregon Revised Statute 468.020 and ORS 468.423 – 468.440 that resulted in DEQ's CWSRF program to begin a transparent rulemaking process to inform how to administer the program properly.

DEQ clarified that there is additional legislation proposed to provide more general funds to help the existing Clean Water Loans program continue to revolve and issue loans. The money requested in the current legislation would be granted and not need to be repaid, which is different from SB 884 and the CWSRF loan funding related to this current rulemaking that must be repaid in order to meet long-term demand.

Summary of key points and discussion

- In 2017, the legislature added an additional \$1.5 million in general fund money for the loan program, now called Clean Water Loans program.
- Craft3 has approved and processed 210 loans.
- Craft3 is responsible for working with loan applicants and certified septic professionals and only defers to DEQ if there is a question of loan project eligibility.
- DEQ clarified that Soil and Water Conservation Districts across the state have the authority to issue loans to repair failing septic systems. Clackamas Soil and Water Conservation District, which is represented on the RAC, is using the CWSRF Local Community Loan for this purpose.

- During committee hearings, the Oregon Senate Environment and Natural Resources committee acknowledged the need for low-interest loans for low-income Oregonians and supported finding creative solutions to the problem.
- DEQ clarified the legislative intent of SB 884 is to assist residents and small businesses who can't access traditional bank loans.

Meeting #2 goals

After background information was provided, facilitator reviewed the goals for this meeting:

- Provide an overview of how CDFIs operate
- Clarify known pass-through lending requirements
- Explore public and private lending to inform CWSRF loan fund impacts
- Solicit input on private lending considerations

DEQ reviewed the RAC milestone timeline and presented an updated meeting schedule, clarifying that session 3 would need to be rescheduled for the first week of June.

Septic system issues and DEQ's program in Oregon

Dave Belyea, DEQ water quality manager, provided a brief overview on current septic system issues and DEQ's programs for residential septic system (onsite) permits and large onsite permits. This presentation can be viewed in the meeting materials for session 2 on the [CWSRF 2020 proposed rulemaking website](#).

DEQ administers two onsite programs, one for residential systems and one for large onsite systems covered by Water Pollution Control Facility permits, known as WPCF. The state is working to have the residential program administered by local jurisdictions. Currently, DEQ runs eight county programs, with counties running the remainder. DEQ operates the WPCF program in all 36 counties. The programs are governed by Oregon Administrative Rules Chapter 340, [Division 071](#), Onsite Wastewater Treatment Systems and Chapter 340, [Division 073](#), Construction Standards.

Summary of key points and discussion

- Large systems are eligible for Clean Water Loans funding
 - Many large systems are owned by individuals, some are large homes, and many are owned by small businesses
- The loans have been readily available and accessed, especially when the situation calls for connecting to a sewer system instead of repair, for which the requirements are articulated in rule
- A failing or failed system can be defined as "not functioning the way it was designed to function"
 - Physical evidence of failure can include visible, seeping sewage or unexplained plant life or marshy-ness on drain fields
 - Often there is no evidence until an existing system evaluation or when adding onto an existing system to find it's not operational
- Most septic systems fail outside the range of sewer systems and must remain as septic
- According to statute, there are three things that make a system eligible for the Clean Water Loan program: repair, replacement, or connecting a failing system to a city sewer
- Residential dwellings, including rentals or secondary properties, or small businesses such as mobile home parks, restaurants and grocery stores, etc., are primary candidates for eligibility
- Loans may not be used for expanding the size of structures or for new developments; the program is focused on septic repair or replacement for existing property owners to stabilize their properties

- A septic system that is well maintained and pumped regularly can easily last 30 years or more depending on soil type. Septic systems that are not maintained can fail quickly.
- The 2,200 septic system repair permits issued in 2018 were reported by owners or neighbors and subsequently repaired.
 - DEQ estimates at least 50 percent of properties continue with failing systems
 - Roughly 10 percent of all systems fail each year as a national average
 - DEQ noted that if a property changes ownership, failing systems will only be reported and addressed if found during an existing system evaluation
 - If a new structure will be roughly the same size as the previous one, it may qualify for a loan.
- In permanent dwelling situations, if Craft3 is unclear about the eligibility criteria, they talk with the homeowner to understand the situation and then consult with DEQ to determine if the situation meets the criteria for a loan
- Emergency situations, like fire or home destruction, can be eligible for loans
- Craft3 loans that DEQ funds are all reimbursable if eligibility rules are met, but if the project is completed without meeting all rules, then the loan becomes ineligible for reimbursement
- Permits can be issued for minor repairs, in most cases the reason for repair is that a system is not operating correctly

Clean Water State Revolving Fund Lending through a CDFI: Overview and Proposed Lending requirements

Overview

DEQ provided a brief overview of CWSRF loan funds passed through a CDFI, possible pass-through lending requirements, and a comparison between current public lending criteria and private lending criteria. This information can be found in the meeting materials and presentation slides for session 2 on the [CWSRF 2020 proposed rulemaking website](#). The purpose of this presentation was to expand on topics from the first RAC meeting and respond to questions to assist the RAC in understanding DEQ's decision-making process.

Proposed pass-through lending requirements

DEQ presented the proposed pass-through lending requirements and how DEQ anticipates the program might work in Oregon. The new and amended rules in chapter 340, division 54, will include alignment with the septic system regulations, including those related to repairs and installation requirements, as outlined in OAR 340-071 and OAR 340-072, that govern the Onsite Wastewater Treatment Systems. Requirements would include:

- Land use compatibility statement showing compliance with Department of Land Conservation and Development land use goals and laws
- Below-market interest rates while ensuring the CWSRF loan fund integrity in perpetuity
 - DEQ will contract with financial consultant PFM to advise on this information
- Loan term that does not exceed the useful life of the asset; currently the average septic system useful life is 20 years
- Project completion triggers repayment
 - The Clean Water Act requires borrowers enter into repayment six months to one year after project completion
 - DEQ will have more information about loan repayment conditions for CDFIS with multiple loans with repair projects at different phases of project completion at the next session
- Principal forgiveness for distressed borrowers and projects meeting green or sustainable criteria
 - DEQ wants to offer debt relief to the end/sub borrower.

- However, CDFIs and septic system repair and replacement do not meet current criteria for principal forgiveness.
- DEQ recognizes the need in Oregon and is consulting with EPA now to address this. DEQ will provide more information at the next meeting.

Summary of key points and discussion

- RAC noted regarding principal forgiveness, it might be helpful to talk with RCAC and Craft3 about their process for when a borrower can't repay their loan. This could inform DEQ's path towards their goals of stewarding funds and positive clean water impacts.
- Craft3 does not foreclose on the property, but charges the payment off on their balance sheet and wait for a recovery when the property sells or use funds from their loan-loss reserve to replenish.
- Craft3 noted that different CDFIs take different approaches. For example, Craft3 will not repossess property, but other CDFIs might. RCAC in Idaho gets a secured deed trust on homeowners' property. Craft3 has thought about grant funds in different capacities, as principal forgiveness can have tax implications for the homeowner. A range of issues can get complicated when allocating grant funds or principal forgiveness directly to a sub-loan as opposed to awarding a grant or principal forgiveness to a CDFI.
- RAC noted another option could be a hardship deferral similar to what SWCDs use. If a borrower shows strong need for a loan they can explain their situation and the district can defer payments, with options for repayment if they are able, on a loan repayment schedule. If local borrower needs to ask for loan modification, they can make a change to the loan.
- A list of current certified CDFIs is available on the [cdfifund.gov website](http://cdfifund.gov).

Comparisons: public vs. private lending

DEQ presented comparisons and considerations around current public lending versus private lending practices. The presentation may be found on the [CWSRF 2020 proposed rulemaking website](#). Topics included:

- General requirements that DEQ would expect from all borrowers
- Financial statements and ratio analysis to evaluate creditworthiness and solvency
- Business and financial management to evaluate ability and willingness to pay
- Security/default remedy to establish the obligation to pay and consequences of non-payment

DEQ staff provided high-level overviews of each topic, and an analysis of current processes and how future CDFI private lending requirements might be implemented. Worksheets were provided as a tool for RAC members to provide feedback, recommendations and concerns regarding the following questions:

- Do these measures seem appropriate to manage risk and evaluate creditworthiness?
- What loan securities should DEQ consider?
- What guaranties might a CDFI make that's comparable to public lending?
- Should DEQ consider credit rating and a minimum loan loss reserve?
- How much weight should DEQ put on ratios?
- What are additional considerations DEQ should consider?

Summary of key points and discussion (verbal and written comments)

- DEQ clarified that loan underwriting guidelines are not in rule, which allows flexibility. Rule language will address the thresholds necessary to protect the loan fund's perpetuity and that are applied to other CWSRF borrowers. This will be discussed more with the financial advisor PFM.

- Loan loss reserve accounts must be restricted. DEQ is not sure yet how to structure reserve accounts for CDFIs.
- CDFIs each have different financial statements. DEQ may need to develop different sets of guidelines to analyze financial statements, which may be complex. DEQ needs to expand how the program will evaluate financial statements and develop underwriting guidelines, which is why DEQ is consulting with an outside financial advisor.
- DEQ wants to include what is needed in rule to clarify and protect all stakeholders, while also allowing flexibility to meet the overall environmental goals.
- It's important to have firm enough rules in place to ensure repayment while flexible enough to not unnecessarily hinder the flow of funding. The program wants to set borrowers up for success while being good stewards of public funds.
- For the past 30 years of the CWSRF program, DEQ has seen only one default.
- DEQ's goal in flexibility is to work carefully and thoughtfully, while the structure is yet to be set.
- DEQ will need to do more research on organizations that rate CDFIs and determine challenges that others have faced. DEQ needs to focus on analyzing the lending operations of non-profit CDFIs in general to ensure any qualifying non-profit CDFI can access the fund. DEQ will discuss coming back to the RAC after initial implementation. DEQ has not reviewed the CDFI rating agency Aeris yet, but plans to do so and to consult with the outside financial advisor to establish appropriate ratios.
- The CDFIs outreach plan must ensure members of the public, particularly in rural areas, are aware of the lending program.
- Stakeholders that could spread the word are contactors, maintenance contractors, installers, designers, health jurisdiction staff, cities, counties, watershed councils, groundwater management boards, and elected officials that focus on water quality. Energy Trust of Oregon's outreach plan is a good model to reference. DEQ doesn't know yet what will be an appropriate collateral security, the actual structure of the loan and how it will be crafted is still in process.
- Regarding security, many CDFIs have non-pledge language with other borrower agreements that limit the CDFI's ability to take on additional debt.
 - DEQ will evaluate debt limitations that most CDFIs experience and determine what is appropriate for CWSRF's security requirements.
 - A letter of credit could be a potential failsafe. The third party consultant will help advise on this.
- DEQ will need to evaluate at least three years of financial statements, at a minimum.
- RAC emphasized it will be a challenge to analyze the financial position, default rate, and the ability to repay of a CDFI. What is the criteria to evaluate a CDFI?
- DEQ will ensure that a CDFI is set up for success and can repay prior to approving a CWSRF loan.
- RAC recommended limiting the amount of loan funding available to CDFIs for the first year or two of implementation given the type of lending and associated risk to the fund are new and must be evaluated to protect the longevity of the loan program. This will allow DEQ the opportunity to mitigate risks related to unknown factors.
- RAC recommended that DEQ reconvene the RAC after the new administrative rules are implemented to review lessons learned and possible rule amendments based on program successes and challenges.

Third party financial consultant: four deliverables

DEQ staff reviewed the need to establish underwriting guidelines for lending to CDFIs. DEQ contracted with a third party financial consulting firm, PFM, to help develop these guidelines with DEQ staff. This firm has worked with many state agencies and works with CWSRFs across the country. PFM will work with DEQ to:

1. Review existing underwriting and collateral policy and procedure
2. Propose security and collateral to be included into underwriting guidelines and future loan agreements
3. Develop a methodology to assess strength of pledged revenue sources and collateral

4. Develop a cash flow model to assess CDFI borrower and sub-loan borrowers' creditworthiness, including modeling potential defaults and remedy, and train DEQ staff on the model

Public comment period

The RAC heard comments and questions from Pat Lando from Recode. DEQ will consult internally on the following questions and respond in writing:

- With the change in scheduling, what about the potential legislative impact and when the legislature is in session.
- Should DEQ be monitoring residential septic systems? What's at risk by continuing to not monitor them? Should the WPCF permitted large onsite systems be monitored more closely? Should more monitoring be written into the CWSRF2020 rulemaking?
- Does this funding have inclusions for onsite sanitation? Why not?
- If these systems are reusing water, onsite non-potable water reuse, as part of an onsite system, is that included in the funding?
- In terms of who is approved for loans, as part of the rulemaking, is there public disclosure on how DEQ is addressing diversity, equity, and inclusion, DEI? The RAC itself does not seem to be representative of DEI.

Post – Meeting Responses to Public Comment and Action Items

Questions	DEQ Responses
With the change in scheduling, think about the potential legislative impact and when the legislature is in session.	The law passed during the 2019 legislative session. This is the rulemaking to implement SB 884.
Should DEQ monitor residential systems? What's at risk by continuing to not monitor them?	This is not within the scope of this rulemaking. However there will be a public rulemaking process for OAR 340-071 and OAR 340-073 to which this topic applies.
Does this funding have inclusions for onsite sanitation, i.e. composting toileting? Why not?	Only if it is allowable under OAR 340-071 and OAR 340-073. CWSRF loans to CDFIs for the purpose of lending to individuals for the repair or replacement of a septic system, and connection to an available sewer, will require borrowers to comply with OAR 340-071 and OAR 340-073.
If these systems are reusing water (onsite non-potable water reuse) as part of an onsite system, is that included in the funding?	Only if it is allowable under OAR 340-071 and OAR 340-073. CWSRF loans to CDFIs for the purpose of lending to individuals for the repair or replacement of a septic system, and connection to an available sewer, will require borrowers to comply with OAR 340-071 and OAR 340-073.
Is there public disclosure on how DEQ is addressing diversity, equity, and inclusion within these rules? With no DEI or minority representation on the RAC, how will DEI be addressed?	RAC members represent statewide public agencies, local governments, local districts and non-profits that serve a diverse set of stakeholders. DEQ's director appointed RAC members that represent stakeholders affected by

Questions	DEQ Responses
	<p>new and amended rules so that they can provide the expertise and advice that will inform new administrative rules that will support implementing SB 884. DEQ expects that each member will represent the interests of their respective constituencies regardless of their own race, ability and socioeconomic status.</p> <p>All eligible CWSRF loan applications are included in the program's Intended Use Plan that DEQ posts to a 30-day public comment period before formally approving the loan application.</p> <p>All CWSRF loan agreements require compliance with anti-discrimination laws.</p>

Rulemaking action items and considerations:

In response to the RAC's questions, DEQ will provide information on the following at the next meeting:

- Determine appropriate below-market interest rates charged to CDFIs and determine what is reasonable for CDFIs to charge to ensure the end user can access the below-market rates
- Determine loan term based on sub-loans and useful life of the asset
- Clarify what principal forgiveness will be available to CDFIs
- Determine if there will be any limits on how much any one CDFI can borrow
- Is DEQ willing to consider a trigger clause to restructure the loan for a CDFI if they have an unanticipated experience?
- What security positions will the state hold? Will that position influence how much DEQ is willing to lend?

Alternative formats

DEQ can provide documents in an alternate format or in a language other than English upon request. Call DEQ at 800-452-4011 or email deqinfo@deq.state.or.us.