Response

On Feb. 8, 2017, the Clean Water State Revolving Fund Advisory Committee asked for additional information for the proposed rule change to 340-054-0071(3), 340-054-0071(5)(b), and 340-054-0065(9). These changes would allow flexibility in refinancing and restructuring loans. The requests are in bold followed by the program’s response.

Refinance is defined as financing debt again, typically as a new loan with a better interest rate, a better term, or both. Currently Oregon Administrative Rule 340-054-0056 - CWSRF Loan Use and Conditions, only allows DEQ to take out interim financing associated with a new project.

Restructure for the purposes of this proposed rule is defined as combining a number of loans into a single larger loan. Currently Oregon Administrative Rule 340-054-0065 - Loan Types, Terms and Interest Rates, allows DEQ to make small changes to loan terms to prevent loss to the program.

Provide information on how communities have responded and inquired about refinancing loans and having their loans combined.

In the last year, two communities asked to have multiple loans combined into one to simplify the repayment process. Both had 20 year terms with similar interest rates. DEQ denied these requests due to current rule.

DEQ proposes to allow combined loans when requested for the borrower’s convenience. This proposal is motivated by a commitment to good customer service, particularly for the most under-resourced communities that can struggle with the complicated nature of the program.

Who does this apply to? When would it make sense to refinance?

DEQ proposes to refinance a loan in the event of prepayments that could harm the program’s perpetuity and the debt obligation of the borrowers, or both. Large prepayments occur on average six to 10 times annually. So far in fiscal year 2017, there have been seven prepayments with two large unexpected prepayments that in total amount to $22 million. Both were due to borrowers seeking better terms.

Could the program refinance a loan from another lender?

DEQ would refinance a loan from another lender only if it is directly related to the project that DEQ is funding. DEQ already has the authority to take out interim or gap financing according to Oregon Administrative Rule 340-054-0065 - Loan Types, Terms and Interest Rates. DEQ does not propose to refinance on a regular basis or when interest rates become lower. Currently DEQ asks borrowers to advise DEQ of other funding that will be combined into the DEQ loan. This would not require any rule change.
Provide better scenarios and describe how this would benefit the community and DEQ.

Refinancing
Once a borrower notifies DEQ that they intend to prepay their loan, DEQ could investigate the benefits of refinancing for both the borrower and DEQ. This would include analyzing the remaining term, interest rate, the total interest and fees paid and compare these to the proposed new terms of the borrower’s intended new debt.

Scenarios that would not merit refinancing would include when a borrower is prepaying debt with accrued funding rather than new debt because they are trying to pay off debt altogether. The same would apply to partial prepayments where borrowers attempt to pay off the loan sooner with accrued funding. These scenarios benefit the rate. DEQ already has the authority to reamortize after a large partial prepayment so no rule change is needed.

Communities would benefit if DEQ were able to refinance a loan for a borrower that intends to prepay their loan with new debt, such as a bond issuance, because the community would save the costs of issuing new debt. If DEQ could negotiate terms that come close to the proposed new debt terms, the borrower would realize savings in interest and fees without other costs. Further, DEQ would benefit because the loan fund would continue to revolve through collecting fees that support the program and avoid the challenges caused by recommitting the repaid loan amount.

Restructuring
The benefit of a combined loan payment to the community is a simpler loan payment plan. The example below shows how two loans could be combined using simple averages. One loan had 38 payments remaining at an interest rate of 2.45 percent and the other loan had 36 payments remaining at an interest rate of 2.88 percent. A weighted average of 2.67 percent would bring the total restructured amounts closer to the original figures for a new term.

<table>
<thead>
<tr>
<th></th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>total amount borrowed</td>
<td>$24,810,545.00</td>
</tr>
<tr>
<td>total amount repaid after term</td>
<td>$24,810,545.00</td>
</tr>
<tr>
<td>total interest paid for 2 loans</td>
<td>$7,907,602.24</td>
</tr>
<tr>
<td>total interest paid for 1 loan</td>
<td>$7,869,339.24</td>
</tr>
<tr>
<td>total fees paid for 2 loans</td>
<td>$1,345,392.00</td>
</tr>
<tr>
<td>total fees paid for 1 loan</td>
<td>$1,337,704.00</td>
</tr>
</tbody>
</table>

Would extended terms be included?
All loan terms could be considered for refinancing and would be evaluated. DEQ could extend and shorten loan terms. Currently most extended term loans are with the most disadvantaged borrowers, who already have the lowest rate that is available. DEQ has not received a prepayment from this type of borrower since the period of 2010-2013 when bond rates were trending much lower than the existing DEQ rates and more than $90 million was prepaid early. This trend has continued to a lesser degree throughout this year. However it is the larger communities with more financial resources that typically refinance their DEQ debt with bonds issued at a lower rate than the existing DEQ rate.
DEQ could negotiate shorter terms that has an associated change of interest rate, much like a home mortgage refinancing from a 30 year to a 15 year with associated increase of payment amount, and a decrease of interest paid.

**Would there be a limit to the number of times a loan could be modified?**

Rather than set a limit on number of times a loan could be modified, DEQ would develop rule language so that any refinance would need to conform to the requirement to support perpetuity. However, significant time and effort is required to refinance debt. It is not likely that a borrower will ask to refinance frequently nor does DEQ propose to refinance a loan several times.

The goal of the proposed refinancing is to reduce prepayment occurrences and keep DEQ’s portfolio loans earning interest and fees for the program. DEQ does not plan to promote refinancing as a program service. Instead the option to refinance if a prepayment is desired by the borrower, will provide a vehicle to improve DEQ’s flexibility to refinance when it is mutually beneficial to the borrower and the program.

The final decision to refinance must rest with DEQ. If financial modeling indicates that a refinance would not benefit the perpetuity of the program, the borrower could proceed to prepay the loan.

**Accessibility**

Documents can be provided upon request in an alternate format for individuals with disabilities or in a language other than English for people with limited English skills. To request a document in another format or language, call DEQ in Portland at 503-229-5696, or toll-free in Oregon at 1-800-452-4011, ext. 5696; or email deqinfo@deq.state.or.us.