



**U. S. Department of Housing and Urban Development
Office of Public and Indian Housing**

Special Attention of:

Public Housing Agencies;
HUD Directors of Public Housing;
PIH Program Center Coordinators;
Public Housing Division Directors;
Regional Directors; Regional
Environmental Officers; Field
Environmental Officers; Regional
Energy Coordinators

NOTICE: PIH-2009-16 (HA)

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Cross Reference:

24 CFR § 85.36;
24 CFR § 965.305;
24 CFR § 965.308;
24 CFR § 990.170;
24 CFR § 990.180;
24 CFR § 990.185.

Subject: Guidance on Energy Performance Contracts, including those with terms up to 20 years

1. **Purpose.** This Notice serves to reinstate and update the content of PIH Notice 2008-22 and provide supplementary guidance regarding retained surcharge savings, approval processing for terms up to 20 years, and the applicability of small purchase procedures for Energy Performance Contracts (EPCs).
2. **Applicability.** This notice applies to public housing and provides guidance under the Public Housing Operating Fund Program pursuant to 24 CFR Part 990 and Energy Performance Contracts pursuant to 24 CFR Part 965, Subpart C.
3. **Effective Date.** This Notice is effective June 12, 2009 and expires June 30, 2010.
4. **Background.**

The Public Housing Operating Fund Program provides funds for the operation and management of public housing. Section 9(e)(2)(C) of the United States Housing Act of 1937 (1937 Act) authorizes public housing agencies (PHAs) to receive the full financial benefit from any reduction in the cost of utilities resulting from any contract with a third party to undertake energy conservation improvements in one or more

public housing projects. Under 24 CFR 990.185, PHAs may qualify for conservation incentives when undertaking conservation measures that are financed by an entity other than HUD, typically through an EPC.

The Energy Policy Act of 2005, Section 151, and the Consolidated Appropriations Act of 2008, Section 229, amended the 1937 Act with respect to energy conservation in public housing. The Department issued an Interim Rule (Federal Register Notice FR-5057-I-01), effective November 17th, 2008, that made conforming amendments to the regulations of the Public Housing Operating Fund Program to reflect these statutory amendments. Effective February 25th, 2009, the Department issued a Final Rule (Federal Register Notice FR - 5057-F-02), accordingly:

- The maximum term of an EPC between a PHA and an entity other than HUD may be up to 20 years; and
- an existing EPC may be extended, without reprocurement of energy performance contractors, to a period of no more than 20 years, to allow additional energy conservation measures (ECMs).

5. Energy Performance Contracting.

Energy Performance Contracting is a financing technique that uses cost savings from reduced energy consumption to pay the cost of installing ECMs. HUD encourages PHAs to employ innovative approaches such as EPCs to achieve programmatic efficiency and reduce utility costs, particularly as PHAs transition to asset management.

The term Energy Services Companies (ESCOs) refers to energy engineering firms as well as other energy engineering consultants hired by the PHA to undertake part or all of an energy project. The term EPC throughout this notice will be used to describe both ESCO and PHA self-developed energy projects.

When using HUD's conservation incentives, the PHA assumes the performance risks for the implemented ECMs. These risks can be mitigated by careful contracting for preparation of an Investment Grade Energy Audit (IGEA) and by prudent project development activities in the energy services agreement (ESA).

When a PHA uses an ESCO, the ESCO prepares the IGEA. With an ESCO, some or all of the projected energy cost savings are typically guaranteed over the term of the financing. PHAs should be aware that guaranteed savings, shared savings, etc., are negotiable provisions in the contract.

A PHA with a self-developed project can retain an energy engineering firm and may purchase an insurance policy to cover its risks. Contract and policy language should be clear, articulating under what conditions losses are collectable under the contract. The IGEA and insurance costs are eligible costs of the project.

The energy and utility conservation measures may include, but are not limited to, the following:

- Water conservation or energy improvements that include repair or replacement of supply pipes;
- Mechanical equipment and systems replacements (boilers, furnaces);
- Thermostatic controls, including programmable thermostats;
- Improvements in building envelope design and function, e.g., penetration sealing, wall insulation, attic insulation, roof replacement, windows, storm doors and vent dampers;
- Lighting and lighting controls;
- Fuel conversions;
- Energy related infrastructure – utility/energy distribution systems;
- Moisture sensing-irrigation systems and controls;
- Green and renewable building technologies, e.g. solar, wind and sustainable design; and,
- Advanced energy savings technologies such as geothermal, cogeneration and water utility technologies such as grey water.

Metering devices alone should not be considered primary energy conservation measures because they measure flow and are not designed to directly reduce consumption. Projected savings based on metering alone often place an unfair burden on residents. The use of meters, however, in conjunction with ECMs, e.g., low flow showerheads, is encouraged. Metering at the utility service level after the installation of ECMs can often save significant utility-related costs through reduced consumption and behavioral adjustments in the user.

Energy and utility conduits alone should not be considered a primary energy conservation measure because they are not designed to directly reduce energy consumption. However, if the conduits are connected to a system that is being replaced or modified as an ECM, repair or replacement of the conduits may be an eligible expense if they will increase the efficacy of the ECM. As with all expenses, such measures will need to be supported with documentation, and are subject to approval by HUD.

6. HUD's Energy Incentives.

A principal advantage to the use of HUD's incentives is that utility savings may be used in lieu of capital funds to finance energy improvements, resulting in lower operating expenses. HUD's incentives offer PHAs the option to direct their capital funds to more emergent as well as long-term modernization efforts and traditional operating funds to operational and management expenses or emergencies. Reduced operating, maintenance and utility costs have a favorable impact on operating ratios and enhance a PHA's credit rating for private investments.

Under an EPC, the PHA may propose to HUD to follow one or more of the four following energy incentives, provided that frozen rolling base, add-on subsidy and

resident paid utility subsidy do not apply to the same ECMs. HUD must approve the use of the incentives, including the length of the contract period. The following incentives are authorized:

- Frozen rolling base (authorized under 24 CFR § 990.185(a)(1)):
- Add-on Subsidy (24 CFR § 990.185(a)(3) and 990.190(b)),
- Resident-paid utility subsidy (24 CFR § 990.185(a)(2)), and
- Rate Reduction (24 CFR § 990.185(b)).

Frozen Rolling Base - A PHA may request that HUD freeze its rolling base consumption to generate savings and allow the PHA to retain 100 percent of the savings from the decreased energy consumption for the term of the contract. With the HUD-approved EPC in place, the rolling base consumption level (RBCL) existing prior to installation of ECMs is used to compute the PHA's Utility Expense Level (UEL) during the term of the HUD incentive period.

For HUD approval of the EPC incentive, the PHA must:

1. submit detailed utility baseline data;
2. verify savings over the term of the incentive using form HUD-52722; and
3. use at least 75 percent of the annual projected utility cost savings to pay project costs, e.g., pay off the debt or bank loan. The remaining 25 percent of the projected annual savings may be used to pay for any eligible operating expense and/or prepay the contract.

Project costs include but are not limited to: equipment, hardware, systems software costs to control and monitor consumption, project design and development costs, training costs directly related to the maintenance, and operation of newly installed equipment.

During the HUD incentive or "performance" period, if less than 75 percent of the projected cost savings is used to pay the debt service on the project costs, HUD will retain the difference between the amortized cost savings used and 75 percent of the projected cost savings.

Add-On Subsidy – An Additional Operating Subsidy (or "add-on") is an increase in total operating subsidy eligibility provided by HUD as a conservation incentive, as described in 24 CFR § 990.185(a)(3)(i). The additional subsidy is for amortization of the loan and contract payment of the EPC and other direct costs related to the conservation project during the term of the contract.

Any approved energy conservation incentive, as is the entire Operating Fund Formula, is subject to annual HUD proration. In the event of subsidy proration, the PHA's year-end savings analysis report will only have to document savings for the amount of the add-on incentive actually received in determining any subsidy offset pursuant to 24 CFR 990.185(a)(3)(iii).

The add-on subsidy is used to amortize the costs of the ECM(s) over time, whether those costs accrue to a bank loan amortization or to pay annual service fees. In addition to receiving the add-on subsidy, the PHA retains cost savings in accordance with 24 CFR § 990.170 as the RBCL continues to be calculated following 24 CFR § 990.180.

The funding period for the add-on subsidy is from January 1st through December 31st of a given calendar year. The PHA may request a partial year add-on subsidy in the initial year of the project. The actual annual savings should be sufficient to cover the costs of the contract, e.g., annual amortization of debt and any mandatory contractor service payments in the same calendar year as the request.

Any shortfall between the actual savings and the add-on subsidy funded for that funding cycle (prorated amount if applicable) will be taken from the next year's subsidy request in accordance with 24 CFR § 990.185(a)(3)(i). The savings verification report for any year of the loan contract will be submitted to the Field Office for review within four months after the end of the (calendar year) funding cycle. This savings verification report will compare the energy savings realized to the add-on subsidy approved for the same time period to determine if an offset against the PHA's operating subsidy eligibility for the PHA's next funding cycle is necessary pursuant to 24 CFR § 990.185(a)(3)(iii).

The burden is on the PHA to coordinate with HUD to ensure that various project periods such as the construction period, financing amortization period and add-on subsidy approval term (HUD incentives period) are coordinated to maximize savings, sufficient to amortize the costs of the project loan and amortized contractor expense.

At the completion of the construction period, the PHA must report to HUD the actual project costs and the post-construction estimates of the savings in consumption and value so that HUD may determine whether any adjustments to the eligible add-on incentive are necessary.

Resident Paid Utilities - PHAs undertaking energy conservation measures that are financed by an entity other than HUD may include resident-paid utilities under the consumption reduction incentive. The PHA must use at least 75 percent of the annual projected cost savings to finance the cost of the improvement.

This incentive allows a PHA to exclude from its operating fund rental income calculations any rents received that are as a result of decreased utility allowances resulting from decreased consumption. The PHA may exclude from its calculation of rental income the increased rental income due to the difference between the baseline allowance and the revised allowances of the projects for the duration of the contract period.

To calculate the amount excluded from rental income after the first year of the EPC contract for the project(s) covered under the contract, the PHA must subtract the

yearly utility consumption from the baseline utility consumption and multiply it by the current utility rate. It is assumed that the number is a positive amount, resulting from a decrease in utilities. This number should be reflected on Section 3, Part B, Line 02 of form, HUD- 52723 (PUM change in utility allowances) as a negative number for each year of the contract term.

Rate Reduction – The rate reduction incentive is included in this notice to provide an all-inclusive discussion of HUD’s incentives.

If a PHA takes action beyond normal public participation and good management in rate-making proceedings, such as well-head purchase of natural gas, administrative appeals, or legal actions to reduce the rate it pays for utilities, then the PHA is permitted to retain 50 percent of the annual savings realized from these actions. No time limit exists on the rate reduction incentive, provided the actions continue to be cost effective.

The rate incentive savings are shared between the agency and HUD and are calculated as the difference between the post- and pre-retrofit consumption times the prevailing and negotiated utility rate. The rate incentive must be calculated each year the agency seeks the incentive. The use of the rate reduction incentive with other incentives has the effect of reducing the incentives at 24 CFR § 990.185.

Use of Excess Savings

In the event that a PHA has completed the terms of an EPC contract and there are excess cost savings after the loan has been paid, a PHA may use any accumulated energy incentive savings as a source of payment for third-party financing of planned energy improvements or for any eligible operating expense of the PHA (24 CFR 990.185(a)(ii)). If the PHA wanted to use excess cost savings for purposes other than eligible Operating Fund expenses, the PHA would need to request a regulation waiver. For example, if the PHA wanted to fund capital improvements with excess cost savings (e.g., entry door retrofits), a waiver of 990.185(a)(ii) must be requested.

7. Contract Period for an Energy Performance Contract.

In an EPC, there are several distinct contract periods associated with:

- Construction;
- Energy Services Agreement (ESA);
- Financing amortization; and
- HUD incentives.

Those contract periods may be discrete timeframes depending on the stages and complexities of the project. For example, the ESA period typically includes the construction period and the financing amortization period. The financing amortization period is typically the same as the HUD incentives period. For the HUD incentives

period, the governing contract period is the approved term (start and completion date) of the HUD incentives, not to exceed 20 years.

Other contract periods related to various energy project stages, such as financing, payback or construction, are not standardized, but should be sufficiently flexible to provide an opportunity to maximize savings and mitigate risk to the PHA.

Regardless of the selected incentive, the PHA must reasonably demonstrate that the savings generated through an EPC will pay for the energy conservation measures and related project costs.

8. IGEA.

A critical initial component of an EPC is the IGEA. The IGEA includes “baseline” utility consumption and cost by utility type, ECMs, estimates of the ECM’s specific potential for reducing utility costs, and the “payback” or time period over which this potential is realized.

An ESCO or energy engineering firm conducts an IGEA of facilities affected by an EPC to determine the potential for energy savings over a utility baseline through such measures as high-efficiency equipment replacements, building upgrades and improved management systems.

The utility baseline in an IGEA must correlate to the three-year rolling base use for the period in which construction initially is to be implemented, as well as the current utility allowance baseline.

The IGEA prescribes a combination of recommended ECMs into an economically viable package. The IGEA also identifies the reasonably anticipated utility savings required to service the debt attributable to the design, development and installation of the combination of ECMs. The utility consumption and cost savings produced by the combination of ECMs included in the energy project must be sufficient to cover all project related costs (including but not limited to such elements as financing, ongoing operations and maintenance services, measurement and verification services, staff and resident training education on energy conservation) over the contract term. Most important for 20-year terms will be the need for savings to persist over the entire term and each year of the energy project.

HUD recommends that PHAs use the International Performance Measurement and Verification Protocol (IPMVP) and American Society of Heating, Refrigerating and Air-Conditioning Engineers (ASHRAE) Guideline 14 as the minimum acceptable levels of analysis in determining utility/energy and demand savings.

9. Measurement and Verification Reports.

Over the life of the contract, HUD recommends that PHAs obtain an annual independent third party savings audit of the measurement and verification report for projects over a total project cost of \$10 million or more. For projects less than \$10 million, an independent savings audit every three years is a cost effective measure to help ensure the persistence and proper accounting of savings over a 20-year term. The cost of the measurement and verification report and any HUD required audit performed by the PHA or independent third party are an allowable expense under a performance contract.

The audit should include reconciliation of actual savings to forms HUD-52723 and HUD-52722 and HUD-approved saving incentives to ensure compliance with contract provisions and projected savings. PHAs should provide a copy of the annual measurement and verification report and, if performed, the independent savings audit to the local Field Office. The PHA's annual submission of the measurement and verification report, audit and reconciliation constitute a certification by the PHA that the savings are accurate, credible, reproducible and auditable.

10. Utility Surcharges.

Some PHAs install check- or sub-meters on PHA-furnished utilities, under an EPC or by other means, to monitor unit, resident or household utility consumption usage. For utility surcharge discussion purposes, resident, household and unit are synonymous. Check- or sub-meters allow PHAs to determine if a resident's consumption has exceeded its utility allowance (UA).

The PHA may, in those cases, charge the resident a surcharge (charge for consumption in excess of the UA) in accordance with provisions in 24 CFR § 965.506 and as acceptable by State and local law. PHAs must also establish schedules of surcharges for excess consumption attributable to resident-owned major appliances or to optional functions of PHA-furnished equipment, e.g., air conditioning.

The PHA must accurately report those surcharges each year to HUD on form HUD-52722, Line 19. (Prior to CY 2007, such surcharges were reported as other income on the old form HUD-52723). There is no reporting exception for PHAs entering into an EPC.

Under an EPC for PHA furnished utilities, a PHA is not eligible to retain resident surcharges as savings to amortize an energy project loan. HUD requires PHAs to report resident surcharges as a component of the eligibility calculation for operating subsidy funds. Utility consumption in excess of the resident utility allowances for PHA-paid utilities is included in the rolling base, part of the basis of a PHA's subsidy eligibility.

The additional funds that the PHA receives from resident surcharges are due back to HUD to offset the cost of utilities paid as part of the operating subsidy. Permitting the

PHA to retain the resident's surcharge and receive reimbursement for the same consumption through the operating subsidy amounts to reimbursing the PHA twice for the same charge.

Beginning with calendar year (CY) 2009 subsidy eligibility submissions and beyond, PHAs that realize additional savings from resident surcharges resulting from EPC projects must report those surcharge savings on form HUD-52722 line 19. HUD will not require PHAs or ESCOs to pay back retained surcharge savings prior to CY 2009. Affected PHAs may need to amend their EPC agreements, as appropriate, to comply with the Department's surcharge requirements.

11. Life Cycle Costs.

Life cycle cost analysis takes into account the long-term economic impact of purchase decisions under an EPC. This information is particularly crucial to HUD and the PHA when considering the project costs over a 20-year contract period. Life cycle cost analysis also assists PHAs in development of appropriate asset maintenance schedules and reducing associated operating costs by identifying potential future repairs.

HUD requires PHAs to provide life cycle cost analysis for proposed systems and equipment when approving an EPC. HUD will only consider providing savings incentives beyond the useful life if a reliable estimate of the replacement cost of the equipment is included in the EPC costs. If the ESCO or energy engineering firm does not contemplate replacing equipment with a useful life less than the contract period, the savings stream from the equipment must stop at the end of its useful life.

For example, with proper preventative maintenance and routine repairs of minor components, furnaces and boilers can be expected to perform 15-25 years; high efficiency air conditioning and central chillers 15-25 years; lighting systems 20 years; toilets and faucets 15-25 years; and refrigerators 6-10 years.

Projects of 12 years and less in duration terminate before most retrofits reach the end of their useful lives. Projects that extend up to 20 years, however, will require some equipment to be replaced midterm. Replacement equipment should be funded through the EPC to the maximum extent possible. If, however, the equipment is replaced by public funds, the PHA must not retain any further energy savings from that equipment.

Any additional operations and maintenance costs due to the ECMs are important considerations in determining long-term project costs, persistence of savings and the life of equipment. Many new green technologies, such as cogeneration, solar and wind technologies require contracted operation and/or maintenance services over the term. Likewise, many pre-existing systems (e.g., older boiler systems) use 24/7 operators and/or outside services contracts and incur large demand charges for energy. PHAs undertaking EPCs with such ECMs should consider having their third party ESCO or engineering firm assess such long-term costs, including costs of providing training for PHA staff in the area of operations, maintenance and repair and/or the cost of outside

service contracts as part of the EPC.

The project expense level (PEL) calculated under 24 CFR § 990.165 includes the cost associated with maintenance, among other expenses. Replacing older, outdated energy equipment should result in maintenance cost savings. The Operating Fund Formula allows PHAs to retain operation and maintenance cost savings under the current PEL calculation. While the maintenance cost savings are not considered utilities, and therefore are not eligible for use in calculating EPC savings, any maintenance savings represent a reduction in operational costs.

- 12. Use of Heating Degree Days.** As applicable, Heating Degree Days (HDDs) or average daily outdoor temperatures may be used by the PHA to demonstrate savings against historic baseline use for weather dependent energy conservation measures. Any HDD adjustment should utilize weather data from the National Oceanic and Atmospheric Administration (NOAA) National Climatic Data Center (NCDC).

- 13. Asset Management.**

Asset management is a management model that emphasizes property-based management as well as long term and strategic planning. PHA transition to asset management is expected to result in greater accountability, more effective use of resources, including utilities, and better quality housing. Energy and water conservation are critical components of asset management. Energy projects that may extend up to 20 years clearly involve a long term, strategic planning component.

Beginning with CY 2007 and going forward, HUD required any new project proposal, IGEA and ESA to present information broken down by project. This requirement is in keeping with 24 CFR § 990.170(f)(2), which requires PHAs to keep utility records at the project level. The required project information should also include: baseline utility consumption and cost correlating to information submitted (or to be submitted) by the PHA in its forms HUD-52722; projected utility consumption and cost savings by utility type, tied to the project utility baseline; the costs of each ECM; cost savings by calendar year for add-on; and, where practical, total savings by incentive type and the total estimated reduction in emissions, e.g., reduced lbs. of carbon dioxide, sulfur, and nitrogen oxide attributable to ECMs and/or lower utility consumption levels.

- 14. Procurement Considerations for Energy Performance Contracts.**

In addition to any Federal requirements, PHAs must comply with any State and local requirements relating to EPCs. For example, if a PHA is subject to a State law limiting EPC terms to 10 years, then the PHA must abide by the State limit, regardless of the higher Federal limit. PHAs should review their State and local laws with their counsel. PIH Directors should consult with Field Office Counsel on conflict of laws questions.

Where permissible, a PHA may use small purchase procurement procedures up to \$100,000 to facilitate the purchase of ECMs, e.g., refrigerators, windows, etc. If there

is a legitimate business or management reason, a PHA can procure similar items separately for each project using small purchase procedures even if, collectively, those items would exceed \$100,000 (the Federal small purchase threshold).

For example, a PHA may begin the year expecting that it needed refrigerators at just one of its projects. Later in the year, the PHA experiences a series of failures at other sites. Combined, the two contracts exceeded \$100,000; however, individually they were both below and within the small purchase threshold. Similarly, a PHA may decide to have individual projects procure separately for heating and cooling maintenance services (even when the total cost of the work would exceed \$100,000) either to support small and minority businesses or because it prefers to have multiple vendors (avoiding the “all eggs in one basket” phenomenon). PHAs should retain documentation to support their business needs.

15. Requests for Extending EPCs Not To Exceed 20 Years.

Effective November 17, 2008, HUD no longer requires a waiver for PHAs who may want a new EPC or to extend an existing EPC to a term of not more than 20 years. The PHA must submit requests for use of HUD incentives directly to the local HUD Field Office for final approval. It is estimated that eliminating Headquarters approval will streamline the EPC process by as much as 4-5 weeks.

PHAs with an existing energy performance contract may request to extend their use of HUD’s energy incentives to a term not to exceed 20 years. The PHA may also initiate a new project using a qualified third party, or terminate their existing contract to take advantage of a new contract with longer terms. If the existing contract is terminated and a new procurement is initiated, the agency may add additional properties for a term not to exceed 20 years to its proposal. The PHA should carefully review the termination clauses in its contract and consider the termination costs.

When considering an extension of an existing contract, the PHA should carefully consider the benefits of procuring or self developing a totally new energy project. For example, a new project can be expanded to include new ECMs for projects under the existing contract in addition to other projects in the PHA’s portfolio. In this instance, the PHA must be cognizant of any activity that may interrupt guarantees and insurance policies on the prior project.

In addition, the IGEA associated with a newly developed EPC project will give the PHA an objective, comprehensive consumption and performance picture of existing ECMs under the original contract and also provides a means for combining other properties and measures not in the original contract. PHA-wide and project-based data provides a more accurate representation of proposed ECM requirements and savings.

Most importantly, under a new project, the PHA can get approval for a contract term not to exceed 20 years versus only a maximum of an additional eight year extension for an existing 12 year contract. The new ESCO or self-developed project can provide larger retained savings for the new contract, resulting from the longer term and open competition among ESCOs, energy engineering firms and energy consultants.

An existing EPC may be extended without the re-procurement of energy performance contractors for only those specific projects included in the original EPC to permit additional energy conservation improvements. For an existing EPC, the PHA must submit its request directly to the local HUD Field Office for approval.

Consistent with the provisions and intentions of Section 229 of the Consolidated Appropriations Act of 2008, the basis for the extension without re-procurement of energy performance contract is the HUD incentives period. Traditionally, enforcement of the contract period has been interpreted as the term of the HUD incentives. From that date forward, the PHA can get approval for extending an existing contract, measured by the HUD incentives period, not to exceed a total of 20 years. The extension term must be continuous with the original term of the contract.

For example, if a PHA requests extension of an existing 12 year contract, the extension must begin at the conclusion of the original incentives period without a break in the incentive period. The PHA can't request an extension, for example, to start one year after the original incentives period ends. The total incentives period must be continuous. The same guidance also applies to self-developed projects.

Documents that would assist the Field Office in its determination of approval include an IGEA for the new project, an amortization schedule, Energy Services Agreement and measurement and verification report and audit that verifies savings have exceeded repayment in the prior 2 years using IPMVP and ASHRAE Guideline 14.

Additional ECMs may be added or replace current ECMs in the original projects as supported by the IGEA. The original utility baseline for each utility type as reported on form HUD-52722 is the basis for the extension. The baseline must be provided by site or project as described in the original contract. Savings from ECMs under the original EPC in conjunction with the savings from the new ECMs in the extension request may be used to amortize the longer contract terms.

For approval, HUD requires PHAs to include in the IGEA life cycle cost analysis, the estimated useful life of the ECMs under the original contract and proposed extension. In addition, HUD recommends that PHAs, as part of its additional energy conservation measures, not replace equipment with more than 30% of its useful life remaining unless it can be demonstrated through the IGEA that replacement is cost effective.

Another way that an EPC can be extended up to the 20-year limit is if the energy cost savings are less than the amount necessary to meet amortization payments specified in a contract. However, this is only possible when HUD determines that the shortfall is the result of changed circumstances, e.g., increase in consumption because of additional rehabbed units coming on line rather than a miscalculation or misrepresentation of

projected energy savings by the contractor or PHA. The contract term may be extended only to accommodate debt service.

16. HUD - Field Office Responsibilities for Energy Performance Contracts.

HUD's role as a reviewer is similar to that of an investor or regulator. As an investor, HUD's interest in the success of the project is minimizing risk to the Department and subsequently, the taxpayer. HUD's role as a regulator is to ensure that PHAs comply with HUD regulations, specifically procurement guidelines and that the HUD incentives period does not exceed 20 years.

In reviewing EPCs for approval, HUD is specifically interested in verifying that projected cost savings generated by the contract will reasonably cover project costs, e.g., the supporting life cycle cost analysis documentation related to projected savings is complete.

24 CFR § 965.308(b) requires that EPCs must be submitted to the HUD Field Office for review and approval before award. In conjunction with a contract review, HUD Field Offices are responsible for reviewing the engineering and financial basis of energy finance projects, processing subsidy requests, and assuring regulatory compliance. Field Offices can expect to spend more review, approval and ongoing regulatory compliance time with 20-year projects and in particular, with requests to extend existing contracts not to exceed 20 years.

Basic documentation provided by the PHA that must be maintained at the Field Office to enable contract performance and regulatory compliance include:

- Request for Proposal;
- Approved IGEA contract;
- IGEA;
- Energy Services Agreement;
- Amortization schedules;
- Affected forms HUD-52722 and HUD-52723 over the life of the contract;
- Annual savings measurement and verification reports and any financial audits with reconciliation to form HUD-52722 or calendar year savings for add-on;
- Correspondence to waiver requests and approvals; and,
- Related change orders or amendments to the initial ESA.

Annually, through the Office of Field Operations, Field Offices will be requested to provide the Office of Public Housing Programs an update of the EPC inventory for HUD's report to Congress, Departmental Energy Action Plan and management goals. Each Field Office will be requested to provide the required cost, consumption and ancillary data in order to meet the Department's annual reporting requirements.

17. PHA Responsibilities for EPCs.

The PHA role in an EPC is that of a business owner, i.e., to negotiate contract conditions in the best interest of the project to ensure project viability and long-term savings. The regulation at 24 CFR § 965.308 requires that PHAs obtain HUD approval of the solicitations for energy performance contracts prior to issuance and prior to award.

PHAs must comply with HUD procurement regulations in 24 CFR § 85.36, which specifically require under 24 CFR § 85.36(c) that all procurement be done in a manner that provides full and open competition. Regulations at 24 CFR § 965.308 and 24 CFR § 85.36(d)(4)(i)(A) require that EPCs be procured through competitive proposals unless services are available only from a single source and justification is provided.

A 20-year contract poses more risk to HUD's Operating Fund if the unit inventory under contract changes. If unit inventory changes due to demolition or disposition for units with an approved frozen rolling base or energy loan amortization add-on, HUD may consider making the appropriate adjustments. The PHA must also consider the impact of such actions on an existing EPC financing agreement.

All EPCs must be submitted to the HUD local Field Office for review and approval before award. PHAs should work closely with their HUD Field Offices throughout the process to ensure common understanding of options, requirements, and outcomes. This interaction should begin during project planning and carry through into project repayment.

At the completion of the construction period, the PHA must report to HUD any change orders or addenda to the ESA occurring during construction. The change order or addenda must clearly evidence changes to the actual project costs and the post-construction estimates of the savings, the latter in both consumption and dollar value. If changes to the approved contract affect the contract cost or the contract savings to the PHA in an amount greater than 10% of the originally approved contract, the PHA must re-submit project documentation to HUD for approval.

EPCs are contracts between the PHA and ESCOs or alternatively energy engineering firms in conjunction with contractors. HUD is not party to these contracts. PHAs, therefore, fully assume the risk for the following:

- (1) Generating sufficient savings to cover payments related to the cost of the energy project; and,
- (2) Savings shortfalls over time attributable to:
 - a) Consumption savings that are not guaranteed;
 - b) Projected rate increases that don't materialize; and,
 - c) Consumption increases that adversely affect the project economics.

HUD encourages PHAs to reduce their risk related to cost and consumption savings to the maximum extent possible through negotiation, guarantees and the use of third party independent consultants.

In particular, PHAs should understand their risks and responsibilities in undertaking an EPC as a self-developed project. A critical aspect for a 20-year term will be the need for savings to persist over the entire term of the energy project. To mitigate risk, a PHA should take into account its capital needs as part of any long-term asset plan and should consider the services of an energy engineering firm, a credentialed independent licensed engineering consultant or certified energy manager when undertaking an EPC.

In the event an EPC project is amended or terminated, the PHA should notify the local HUD Field Office immediately, detailing the conditions and causes of the amendment or termination.

18. Conflicts of Interest.

If in-house expertise is not available, HUD recommends that housing agencies consider hiring qualified engineering and financial contractors for assistance. All procurement transactions will be conducted in a manner providing full and open competition consistent with the standards of 24 CFR § 85.36.

No third party contractor to the PHA will participate in the selection, award, or administration of a contract supported by Federal funds if a conflict of interest, financial or otherwise, real or apparent, would be involved. Such a conflict would arise when the contractor, officer or agent, any member of his or her immediate family, his or her partner, or an organization which employs or is about to employ any of the above, has a financial or other interest in the firm selected for the award.

A perception issue also arises when a consulting firm, e.g., financial, working for an energy engineering firm also worked for the housing agency and uses their former relationship with the housing agency to give preferential treatment or conditions that better serve the energy engineering firm without proper negotiation.

The consulting firm must provide a certification to the PHA with a copy to the local Field Office that a conflict of interest does not exist. For more information, see the Procurement Handbook 7460.8 Rev 2 paragraph 4.4.

HUD encourages energy engineering firms and other third party consultants seeking to help PHAs reduce energy consumption to market their services, products, qualifications and expertise in energy conservation. They, however, must refrain from any activities that involve paid or free technical assistance specifically related to the preparation of energy procurement documentation, such as a statement of work or request for proposals/qualifications for which their firm may directly or indirectly compete for an award.

All procurement transactions will be conducted in a manner providing full and open competition consistent with the standards of 24 CFR § 85.36. No firm may participate in the preparation, selection, award, or administration of a contract supported by Federal funds if a conflict of interest, financial or otherwise, real or apparent, would be involved.

19. Further Information. Direct inquiries to Dina Elani, Director, Office of Management and Occupancy at (202) 402-2071. Direct requests for technical assistance related to audits, procurement, training, templates or other energy guidance to the local HUD Field Office. HUD's Public Housing Energy website is <http://www.hud.gov/offices/pih/programs/ph/phecc/epformance.cfm>.

20. Paperwork Reduction Act. The HUD forms referenced in this notice are approved under the Paperwork Reduction Act - OMB Control Number 2577-0029.

/s/

Paula O. Blunt, General Deputy Assistant Secretary
for Public and Indian Housing

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