Joint Comments
to the United States Department of Agriculture
on the
Rural Development Grants Proposed Rule
73 Fed. Reg. 61198 (October 15, 2008)*

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(additional signatories added December 23, 2008)

I. Introduction and Summary of Comments

Our organizations are pleased to submit the following comments to the U.S. Department of Agriculture on the Department's proposed rule on Rural Development Grants, 73 Fed. Reg. 61198 (Oct. 15, 2008). These comments focus on the proposed changes to the Rural Energy for America Program (REAP).

When Congress provided its strong support for expanding and enhancing this program in the 2008 Farm Bill, it made clear in its legislation and the Managers' Report that:

- The program should be streamlined and simplified as much as possible.
- The program should serve a wide range of technologies, in a wide range of sizes.
- The program should support sound project planning by providing funds for feasibility studies.
- Projects that convert animal manure to energy, including both on-farm and community projects, should receive support.

Notably, nothing in the statute or legislative history suggests that Congress intended to condition larger grant applications on first obtaining loan guarantees, as USDA has proposed to do here.

While limited aspects of USDA's proposal may meet Congressional intent for REAP, we are concerned that other aspects will frustrate Congressional intent. Therefore, we recommend several changes to the proposal, including these listed below and others explained in these Comments:

- Eliminate the common grant platform and continue to implement these grant programs on a program-specific basis. There are simply too many differences among the programs for consolidation to achieve the intended efficiencies.
- The requirement of a loan guarantee application for grant requests over $50,000 is contrary to the statute, creates an unwarranted bias against grants for medium-sized and larger projects and puts the decision-making power partially in the hands of bankers who may or may not submit loan guarantee paperwork.

- The continuing exclusion of non-rural agricultural producers for this program, such as greenhouses, is contrary to Congressional intent for the REAP program and prejudices producers, such as greenhouse growers, in formerly rural areas.

- The Department's proposed "Priority List" of ranking projects may discriminate against larger projects and against projects with other public funding and should be eliminated.

II. General Comments

In general, we are concerned that the proposed consolidation does not achieve its intended purpose of increased efficiency. For a net gain in efficiency from the perspective of the applicant, the two layers of program rules need to be invisible to the applicants and the rules succinctly and clearly presented. The separation of the rules into Subparts A and B, with Subpart B provisions sometimes modifying and qualifying Subpart A provisions, is confusing. Creating separate deadlines and other specific conditions for each of the programs undermines the goal of harmonizing all of the rules. Distinguishing between programs with open application periods and fixed application deadlines adds an additional level of distinction. In some cases the Department simply omitted large amounts of information previously included in the program rules (for example, the technology-specific information for REAP applications), rather than consolidating with other program requirements. For these reasons, we encourage USDA to drop the common platform proposal and instead focus on improving each program's application process, especially through streamlined applications and much more use of web delivery services (for which USDA does not yet have a strong track record).

III. Comments on Subpart A (General Provisions)

Although we recommend that USDA drop the common grant platform and the General Provisions in Subpart A, we do recommend several changes to these provisions that USDA should incorporate in final REAP-specific rules.

A. Notifications – Needs More Publicity

We are concerned with how USDA proposes to alert the public to the Notifications for nationally-administered programs such as REAP. USDA intends to publish these Notifications only in the Federal Register and plans to make them available at Rural Development offices. Instead, USDA should issue news releases, publish all program Notifications for REAP in the Federal Register and in a dedicated REAP section on the Department's Web site. (This also would be similar to the Department's proposal to make Notifications for State-Allocated programs available on its Web site.) The Federal Register is not a commonly-read publication for the general public, and USDA should promote REAP and the other large national programs through all available means, including its Web site as well as at Rural Development office.

We also are concerned with the Department's proposal regarding timing of the Notifications. USDA has proposed to release the program funding level and grant limit information "each fiscal year," (§ 5002.15(d)(1)), but the regulation does not specify *when* in the fiscal year USDA will release the information. We recommend that the USDA release this information no later than 30 days after the start of the fiscal year.

As a related matter, USDA has proposed to include the "funding level" in the Notification. We do not understand how the Department will always know the funding level early in the fiscal year, since Congress rarely passes appropriations bills on time. Since a major purpose of USDA's proposed rule is to decouple the appropriations process from the application process, we urge USDA not to delay the Notification process pending confirmation of the Congressionally-determined funding level.

USDA has also proposed to release updated information on the Administrator and State priority categories and point allocations at least 30 days prior to the first ranking or application date. Given that many applicants may submit their applications more than one month prior to the relevant ranking or application deadline, USDA should significantly lengthen the timing of the release of this information. Ideally such information should be available at the same time early in the fiscal year that it releases the minimum and maximum grant funding levels.

B. <u>Preapplication Process – Needs Additional Detail and Certainty</u>

USDA's proposal to accept "preapplications" to determine whether applications meet applicant and project eligibility requirements is a good idea but needs to be simplified and conducted on a continuing basis. USDA has not proposed any application criteria for the preapplication process, nor has it specified a deadline by which USDA will act on preapplications. Therefore, USDA should:

- Allow applicants to submit pre-applications throughout the year, up to a reasonable final deadline (for example, March 15);
- Specify the preapplication requirements; and
- Commit to acting on preapplications within a reasonable date (we recommend 30 days) after receipt.

In particular, responding to preapplications by a date certain will inform applicants in a timely manner whether they should proceed with the full application.

C. <u>The Application Process – Improve Publicity and Remove USDA Discretion</u>

We recommend two changes to the proposed application process. First, the Department's Web site should serve as a primary source for all application forms and other required information, together with Rural Development offices. USDA has proposed only to make those forms available at Rural Development offices.

Second, USDA proposes to initially screen applications according to the standard of whether they are "feasible or likely to be feasible with regard to financial, technical, and environmental feasibility and sustainability of the project" (§ 5002.40(a)). That standard, which is not in the authorizing statute, vests significant discretion in USDA and the proposal offers no objective criteria for evaluation. Given the lack of any standard of feasibility, USDA should eliminate this requirement from the proposal.

D. <u>Ranking Applications – Second and Third Criteria Are Unnecessary</u>

USDA has proposed to rank grant applications and create a "Priority List" of projects for funding when funding becomes available. USDA proposes three criteria for ranking applications and selecting them for funding/potential funding. The first criterion—higher ranking scores—clearly makes sense and is appropriate. As we explain below, the other two criteria do not make sense and should be eliminated. Therefore, the ranking list should consist only of the top-scoring applications.

The problem with the second ranking criterion—the size of the request relative to grant funds—is that it could create a deterrent against larger projects, especially when judged in isolation. For example, if $500,000 remains in the funding account for REAP, and the four highest-ranking applications are valued at $350,000, $150,000, $100,000 and $100,000, will USDA reject the $350,000 application in favor of the other applications? That seems unreasonable, especially if the higher-value application was submitted earlier in the year, or if it provides greater clean energy produced or saved relative to the investment of program dollars. USDA therefore should remove this criterion.

As for the third criterion—availability of other funds—USDA explained it in this way:

> ***Availability of other funding sources.*** *This refers to whether Rural Development loans and other, non-Rural Development funding sources should be available to an applicant. If an applicant with a higher-scoring application can accomplish the project using Rural Development loans or other non-Rural Development funding sources, the Agency may consider the next highest scoring application ahead of the higher scoring application.*

73 Fed. Reg. at 61212.

In the past, USDA Rural Development factored in a project's ability to procure additional funds from other sources (cash in hand, investors money, liquid assets, etc.) as part of the Department's evaluation of an applicant's worthiness for receiving a USDA-RD REAP grant, partly because the grant program was intended to be more of an *incentive* to stimulate new projects and not just a *subsidy* for overall capitalization. Therefore, the Department traditionally applied criteria in grant scoring that asked, essentially, "Does the project have adequate financing to carry it to fruition, if a USDA-RD grant is received?" And in general, the Department has viewed its Rural Development loan programs as a *complimentary* way to fund a project and *extend* its other sources of overall capital, beyond the initial grant funding it needed.

As written, however, the new criterion is problematic for several reasons. First, it adds another layer of needs testing beyond what already is in the REAP scoring system. USDA proposes to take financial need into account by adding up to five points to grant applicants who can demonstrate financial need. 73 Fed. Reg. at 61244. Therefore, the ranking proposal would push those applicants who cannot demonstrate financial need even further down the list.

Second, it is very unclear as to how the Agency intends to consistently determine "[i]f an applicant … can accomplish the project using (RD) loans or other non-Rural Development funding sources …." It is already a challenge for the agency to consistently rank projects' capitalization 'fitness' level without also attempting to judge the project's likelihood of qualifying for other USDA-RD programs (i.e., the RD loan programs) in the future, let alone non-RD programs. And many state programs are intended to complement REAP funding, especially given REAP's comparatively low 25% maximum grant cost-share.

Third, the proposal could reposition the USDA Rural Development loan program as a competing source of project financing within its own program area, rather than as a complementary source. The USDA-RD grant programs are set up to provide a relatively small incentive to create new projects when applicants cannot handle 100% of the initial start-up capital and risk, while the loan programs are set up to provide a small incentive for banks to lend additional capital to these projects. The proposal creates confusion and conflict for the applicant, by creating a “trade off’ between the grants and the loan-acquisition subsidies.

In summary, most of the problems with the proposed ranking system appear to result from USDA’s proposal to combine requirements in the common platform (Subpart A) with REAP-specific requirements. This provides another reason why the proposed common platform is unnecessary and will create more confusion than efficiency for grant applicants.

Separately, we urge USDA to release the Priority List of grant applications on the Department’s Web site and through other means as soon as USDA completes the list. Transparency is critical to maintaining the integrity of the application process, and since the Priority List will determine whether projects receive funding, all applicants and the general public deserve to see the results of the ranking process. This can be done while protecting applicants’ competitive and confidential information.

IV. Comments on Subpart B (REAP-Specific Provisions)

A. Loan Guarantee Requirements – Eliminate It

USDA has proposed to reject applications for grants of more than $50,000 unless the applicant cannot obtain a USDA loan guarantee for any portion of the project, or if the grant amount is necessary for a bank to make a guaranteed loan to the applicant. We strongly object to this unsupported proposal for several reasons. We also note that during these extremely challenging economic times, the continuing unconditioned availability of grants will be critical to projects moving forward.

Despite clear calls from the community for USDA to drop its preference for loan guarantees, this policy actually hardens the preference. Although the USDA has tried for years to prioritize loan guarantees—the public has clearly rejected this preference—since loan guarantees continue to represent a relatively small fraction of total award dollars.

The $50,000 cap on grants also is contrary to the statute, which treats grants and loan guarantees equally and does not create any preference in favor of loan guarantees. (For example, the Farm Bill managers' report clearly calls for "significant support" for on-farm and community digesters, which this policy would undermine.) While Congress included directions to the Secretary that at least 20% of program funds go to projects with grants under $20,000, it implicitly approved of 80% of funding going to larger projects, whether in the form of grants or loan guarantees.

We also are concerned that this proposal delegates too much authority to private sector bankers who must agree to prepare and submit loan guarantee paperwork, and to accept the terms of the loan guarantee. Acceptance of loan guarantees by the banking community has varied remarkably from state to state, and far more than grants, loan guarantee awards have been heavily concentrated in several states.

As a practical matter, this proposed rule likely will leave large amounts of REAP program funds unused as it drives away larger projects such as digesters and community wind, especially as demand for REAP loan guarantees is not nearly as strong as USDA had predicted. In many cases loan guarantees simply are not sufficient to ensure that a project moves forward, which is why REAP includes the grant option, regardless of size. The lost clean energy production potential is too high a cost to pay for whatever goal the USDA seeks to achieve with this rule.

In summary, this proposal is contrary to Congressional intent, will reduce program reach and effectiveness and will result in less overall program success. USDA therefore should eliminate this requirement entirely from the program.

B. Project Eligibility – Rural Area Requirement Is Unreasonable

USDA proposes to continue to limit eligibility for the REAP program to projects located in a rural area, (§ 5002.102(b)(1)(ii)), even though the 2008 Farm Bill expanded the program to include all agriculture producers, including those in non-rural areas. Previously, the Section 9006 program as created in the 2002 Farm Bill applied to “farmers, ranchers and rural small businesses.” Under the USDA interpretation of this definition, greenhouses, nurseries and other producers located in non-rural areas were excluded from eligibility for Section 9006 grants and loan guarantees.

The legislative language in Section 9007 of the 2008 Farm Bill deliberately expanded the scope of the renewable energy and energy efficiency grant and loan guarantee program to include all “agricultural producers and rural small businesses.” (§ 9007(c)(1)). Under this new statutory provision and USDA definitions of “agricultural producer,” the Department should recognize that that any greenhouse or nursery operation, and any other non-rural agricultural producer, is eligible for the grant and loan guarantee program, *regardless of location*. If Congress wanted to restrict agricultural producers to just rural areas, it would have added the “rural” limitation as it did with “small business.”

USDA’s continuing restriction of the REAP program to only agricultural producers in rural areas is not equitable for non-rural agricultural producers, especially those that are located in formerly rural areas that are now “non-rural” due to population shifts. For example, as many as two-thirds of the greenhouse growers in Northwest Ohio are from Lucas County (Toledo metro area) and are disqualified from participating in the program.[1] Moreover, there is no other statutory limitation on USDA’s ability to include non-rural agriculture producers in the REAP program. Therefore, USDA should expand the REAP program to include non-rural agriculture producers.

C. <u>Project Eligibility – Feasibility Study Standards Are Missing</u>

USDA proposes to allow feasibility studies as eligible grant projects. (§ 5002.102(b)(2)). Beyond that one-sentence provision, however, USDA has provided no guidance on standards for evaluating applications for feasibility studies. Therefore, we recommend that USDA issue interim standards for feasibility studies in a Notice of Funds Availability for the FY2009 program, and then issue a supplemental proposed rule that addresses feasibility studies in more detail.

D. <u>Application and Processing Deadlines Are Confusing</u>

The Department’s proposed application deadlines are confusing and incomplete. We would prefer a rolling application deadline process in which USDA makes decisions within some period of time (for example, 30 days) after receiving an application. Alternatively, if USDA chooses to use deadlines, it should clarify how it will process applications.

USDA has proposed two “ranking” decision dates of March 15 and July 15, and one application deadline of June 15. One could infer from these dates that USDA will score all applications received by June 15 within 30 days – by July 15. If that is the case, USDA should be similarly clear with the earlier ranking deadline of March 15, and provide an earlier first application deadline date of February 15. In that case, the deadlines would be:

February 15 – application deadline
March 15 – ranking date

June 15 – application deadline
July 15 – ranking date

We also recommend that USDA add two additional sets of ranking and application dates, identical to its proposal in the Subpart A general requirements section for open applications (73 Fed. Reg. at 61211). Those dates would be:

November 15 – application deadline
December 15 – ranking date

July 15 – application deadline
August 15 – ranking date

Creating four deadlines would move the program more closely to use a rolling application process. And in all cases, USDA would roll over to the next application period those applications that miss a deadline (except for the final application deadline for the year). Applicants also need to understand that waiting until late in the year may reduce their chances of receiving a grant award, as USDA may expend all grant funds by then.

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[1] See Letter from Maumee Valley Growers to USDA regarding the Energy Title Rulemaking (Sept. 19, 2008).

E. Simplified Applications – Needs Standards

Although USDA has proposed a simplified application process, it has not proposed any requirements for the process. Instead, the Department states that most of the requirements will be available at Rural Development offices and on USDA's Web site. Without knowing these standards and requirements, however, we cannot comment on the simplified application process. The current Section 9006 rules include simplified application requirements (7 CFR § 4280.109). The Department should similarly propose these or other standards so that the public can comment on them.

F. Administrator Priority Categories – Eliminate or Reduce Points

USDA created the new Administrator Priority categories for national lead programs such as REAP, in an effort to limit the Administrator's current "significant discretion to reflect their priorities." 73 Fed. Reg. 61320. According to the proposal, adding explicit Administrator categories (and State Director categories, for state lead programs) will "provide the public with much greater understanding of how their applications can be evaluated by the Administrator and State Directors.") *Id.*

The USDA has proposed several Administrator categories for the REAP program, including: unserved or underserved areas; geographic diversity; emergency conditions; public health and safety; and emergency directives. 73 Fed. Reg. at 61244. USDA intends to award up to ten points for Administrator categories.

We support the Department's effort to limit its discretion to award grants for reasons other than those listed in the rules/guidelines and annual Notices of Funds Availability. Indeed, we encourage the Department to completely remove its discretion and eliminate the Administrator Categories, at least as applied to REAP grants. Alternatively, if USDA decides to retain Administrator Priorities, we urge USDA to reduce the number of points from ten to five. Ten points is a significant number of points in the Department's 100 point scoring section, and often is the difference between a successful and unsuccessful application. Ten points also is large relative to other categories. For example, ten points is more points than the Department proposes to award for financial need, return on investment, small agricultural producer, commercial availability, and environmental benefits. We also believe that as applied to REAP grants, only two of the five Administrator Categories are likely to be relevant: underserved areas, and geographic diversity. Accordingly, we urge USDA to reduce the total number of Administrator Priority points to no more than five points.