The standard loan term is 20-years and can be up to 30-years for projects that meet the disadvantaged community criteria described in Section I below. No loan term can exceed the useful life of the project.

In order to manage large project requests within the DWRF annual lending capacity, the PFA may provide separate financing agreements for some projects over more than one year based on the project's cash flow needs as negotiated between PFA and the borrower.

H. Loan Terms and Conditions - Lead Service Line Projects (Public Portion)

Terms and conditions for DWRF lead service line loans are established under Laws of Minnesota, 2023, Chapter 39, Section 2 (which will be codified into Minn Stat 446A.081, Subd 8 (h)). The interest rate on the public portion of the lead service line project will be at 0.00% with principal payments commencing not later than 18 months after the completion of the project. The term for LSLR loans is 10 years. PFA financing agreements will include a provision that prohibits assessing property owners for any cost of the lead service line replacement.

Also, refer to Section L for information on the State Lead Service Line Replacement Grant program including details on grants for a portion of the public side and priority use of state grant funds to repay the public side DWRF loan.

I. Additional Subsidization

The federal capitalization grants require a certain percent of the funds be used for additional subsidization of projects meeting specific criteria beyond the below-market interest rates on loans described above. The PFA provides additional subsidization to eligible projects in the form of Principal Forgiveness grants, meaning a specific dollar reduction in the amount of loan principal that must be repaid, which is granted at the time a DWRF financing agreement is awarded. The PFA will award Principal Forgiveness grants to address affordability, replacement of lead service lines, and for projects that address emerging contaminants. Estimated federal principal forgiveness and WIF calculations for carryover projects are reflected on Table 1a and Table 1b.

Minnesota Statutes, Section 446A.081, Subdivision 9, as amended by Laws of Minnesota 2023, Chapter 39, Section 5 (Chapter 39 - MN Laws) authorizes the PFA to provide Principal Forgiveness to the extent permitted under federal law.

1. Disadvantaged Community Principal Forgiveness (affordability)

The PFA received the 2023 base capitalization grant in September of 2023. The 2023 base grant is $7,470,000 and requires a minimum of $1,942,200 be used for additional subsidization. The PFA also has $18.9 million in additional subsidization funds available from prior federal funds.

The IUP Table 1a shows $18.6 million in estimated carryover projects that are eligible for disadvantaged community (affordability-based) principal forgiveness. New project requests will be reviewed for principal forgiveness affordability after loan applications are submitted.

Disadvantaged Communities are defined by the affordability criteria of the Minnesota State Water Infrastructure Fund (WIF) criteria further detailed in Section J.

Principal forgiveness and state Water Infrastructure Funds for affordability are reserved and awarded to eligible projects based on their PPL ranking, beginning first with carryover projects (that received technical approval and certification in a prior fiscal year), followed by new IUP projects. If sufficient grant funds are not available, a project may remain on the IUP as a carryover project and eligible funding will be reserved and awarded when new appropriations are available.

2. *Emerging Contaminant Principal Forgiveness*

The PFA has $12 million available in principal forgiveness funds for Emerging Contaminant projects from prior federal funds. The IUP Table 1a shows $2.4 million in estimated principal forgiveness for carryover projects and $21.3 million for estimated principal forgiveness for new EC project requests.

Chapter 39 - MN Laws (2023) set federal principal forgiveness at 50% up to a maximum of $3,000,000 for emerging contaminant projects. Principal forgiveness for Emerging Contaminant projects are reserved and awarded for projects based on their PPL ranking, beginning first with carryover projects (that received technical approval and certification in a prior fiscal year), followed by new IUP projects. If sufficient principal forgiveness funds are not available, a project may remain on the IUP as a carryover project and eligible funding will be reserved and awarded when new appropriations are available.

3. *Lead Service Line Principal Forgiveness (Disadvantaged Communities)*

The PFA has $21.2 million available in principal forgiveness funds for Lead Service Line Replacement projects from prior federal funds. Table 1b shows $16.3 million estimated principal forgiveness for LSLR carryover projects. New project requests on Table 1b, Part B exceed $76 million in requested LSLR funding, and all new project requests will trigger principal forgiveness at some level for the project.

Federal principal forgiveness funds will be used for private lead service line replacement costs for disadvantaged communities. See Section K for additional details. Statutory changes (Chapter 39 - MN Laws) enacted in 2023, modified the principal forgiveness for lead service line projects by eliminating the funding cap, and establishing 0% interest for LSLR loans. A new state lead service line replacement grant program (Chapter 39 - MN Laws) was established and funds appropriated. See Section L for additional information on the State's LSLR grant program. The federal LSLR funds, including principal forgiveness funds, will be coordinated with the State's LSLR grant program.

4. Coordination of Federal Principal Forgiveness and State Grant Funds

Principal Forgiveness and available state WIF funds will be used to address affordability needs for regular projects and the source of funding for each project (federal Principal Forgiveness or state WIF funds) will be determined at the time of award.

Federal LSLR principal forgiveness funds and state LSLR grant funds will be used to address LSLR projects and the source of funding (federal and/or state) will be determined at the time of grant award.

J. Disadvantaged Communities – Affordability for Regular and Emerging Contaminants (loan portion) Projects

Minnesota has established its state-funded Water Infrastructure Funding (WIF) grant program in [Minnesota Statutes, Section 446A.072] to help municipalities build projects to replace aging and obsolete water systems that would otherwise create a significant financial hardship for the municipality. The methodology looks at the financial impact on municipal users if the municipality had to finance the project with only DWRF loan assistance. The financial criteria considers the total system costs including: annual operation and maintenance costs, annual debt service for prior capital improvements and projected new debt service for the proposed project based on the maximum allowable loan term. The financial impact is determined by dividing the total system costs by the number of residential users (measured by equivalent residential units) to determine the average cost per household. If the average cost per household exceeds 1.2% of the service area's median household income (MHI) the proposed project is considered to create significant hardship.

Minnesota uses the WIF grant affordability criteria to identify disadvantaged communities that are eligible for DWRF Principal Forgiveness and/or WIF grants. The same criteria will be used for the DWRF loan portion of Emerging Contaminants projects not covered by EC principal forgiveness funds. The amount of Principal Forgiveness or WIF grant funding is limited to 80 percent of the system costs over 1.2% of MHI, to a maximum of $5,000,000 or $20,000 per connection, not to exceed 80 percent of the total project cost. Disadvantaged community projects qualifying for Principal Forgiveness or WIF grants cannot be determined based solely on information provided in the IUP request. Additional project information submitted during the application phase, including details on system users and system costs, debt service and as-bid costs are necessary to calculate the cost impact to system users and whether the project triggers the disadvantaged community criteria.

When funds are available, the PFA reserves WIF grants and Principal Forgiveness funds for eligible DWRF projects when they are certified by the MDH. Funds are reserved in an amount based on the cost estimate when the project is certified or the as-bid cost, whichever is less. If sufficient WIF grants and PF funds are not available when a project is certified, the project may remain on the IUP as a carryover project and eligible funding will be reserved when new funding appropriations are available.

K. Disadvantaged Communities – Lead Service Line Replacement (LSLR) Projects

Federal IIJA funds provide a new source of funding to address lead service lines, with 49% of the funds available as Principal Forgiveness for disadvantaged communities. Recipients of LSLR funds must replace the entire lead service line, not just a portion, unless a portion has already been replaced or is concurrently being replaced with another funding source.

In 2023, a new state Lead Service Line Replacement Grant program was established and $240 million appropriated for lead service line replacement work (Chapter 39 - MN Laws). The state program structure will maximize and work in conjunction with the federal IIJA LSLR funds. Up to 10% of the appropriation ($24 million) may be used for lead service line mapping and inventory costs.

PFA has carefully reviewed how its disadvantaged community definition will apply to lead service line projects. A significant portion of a drinking water service line is owned by the property owner and municipalities cannot use system revenues to pay the cost to replace the privately owned portion. Generally, special assessments to each individual property owner have been the only way to pay the private portion of the lead service line replacement cost, resulting in the cost impact falling on each property owner rather than over a municipality's entire user base. This can result in significant costs to each property owner that may often be an affordability barrier to replacing the lead service line.

PFA has determined it is appropriate to focus on the financial impact to the property owner rather than the municipality as a whole. For IIJA-funded lead service line replacement projects, PFA will determine what the estimated annual cost would be for each property if the replacement of the private portion were financed through a special assessment on the property over ten years. PFA will then add the average cost per household for water service (reflecting the operation and maintenance and debt service costs of the system) and compare the total to the municipality's median household income. If the result exceeds the established 1.2% threshold, the municipality will be considered a disadvantaged community and the lead service line replacement project will be eligible for federal principal forgiveness.

When a city applies for a LSLR project, the PFA will review the applicant's current water rates and estimated cost to replace the private portion of the lead service line and calculate the total cost impact on the property owner. If the costs are over 1.2% of the median household income, the applicant's community is identified as a disadvantaged community and eligible for federal principal forgiveness for the private portion of the lead service line.

If the costs are below the 1.2% MHI threshold, the PFA will discuss with the city targeting the LSLR project to specific census tracts and then using the census tract MHI to determine disadvantaged communities within the municipality that are above the 1.2% MHI threshold. A combination of State LSLR grant funds and DWRF LSLR loan funds will be used for those public water systems that do not meet the established affordability criteria.

The State Lead Service Line Replacement Grant program requires removal and replacement of the privately-owned lead service line at no cost to the property owner.

Principal forgiveness or state grants for LSLR projects will be available for projects that have partial or full private ownership of the line. Public-side costs of LSLR projects not covered by the State LSLR grant program will be funded with an IIJA LSLR DWRF loan. The Minnesota LSLR Grant program provides up to 50% grant for the public-side of LSLR projects. In addition, the first priority for the state LSLR grant funds is to pay debt incurred for the project on the publicly funded DWRF loan.

L. State Lead Service Line Replacement Grant Program

Minnesota established a new state funded Lead Service Line Replacement Grant Program in May 2023. The state set a goal to remove all lead service lines in public drinking water systems by 2033 and appropriated $240 million for the grant program. The State LSLR Grant program is separate state program that was designed to maximize the use of the federal IIJA lead service line funding. The two funding sources will be closely coordinated, and both are managed by the PFA and MDH.

The State Lead Service Line Replacement Grant Program requires that:

- all eligible recipients be listed on the MDH's Project Priority List;
- state grant funds pay 100% of the cost of replacing the privately owned portions of lead service lines;
- state grant funds pay for not more than 50% of the cost of the publicly owned portion of the lead service lines;
- state grant funds will first be used to repay DWRF debt incurred for the public side of lead service line replacement projects.

M. DWRF Federal and State Requirements

DWRF-funded projects are subject to both federal and state requirements. Additional information on the requirements are detailed in the PFA application materials and Contract Packet which are available on the PFA website.

The IIJA signed into law November 15, 2021 (Public Law 117-580) included additional Drinking Water State Revolving Fund requirements. Build America, Buy America (BABA) Act is a new