

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 DWRP 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 DWRP Principal Forgiveness and/or WIF grants. The same criteria will be used for the DWRP 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 DWRP 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 IJJA 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 IJJA 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 IJJA-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 DWRP 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 IJA LSLR DWRP 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 DWRP 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 IJA 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 DWRP debt incurred for the public side of lead service line replacement projects.

#### *M. DWRP Federal and State Requirements*

DWRP-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 IJA 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

domestic sourcing requirement for federal financial assistance programs for infrastructure. An earlier EPA approved Adjustment Period Waiver has been amended which places limitations on which projects qualify for the waiver. Consult with your loan officer and MDH for additional information.

**III. Summary of FY 2023 Project Activity**

A total of 24 municipal drinking water projects on the 2023 PPL totaling \$44.3 million were funded in FY 2023 through the coordinated efforts of the PFA and other funding partners.

**IUP Drinking Water PPL Projects Funded In FY 2023**

Project Name	PPL Points	Project Description	Project Cost (\$)	DWSRF Loan (\$)	DWSRF PF (\$)	Other Funding (\$)	Other Source
Annandale	10	Watermain-Repl Oak, Park, Pleasant	1,358,413	1,358,413	-	-	
Bemidji	10	Treatment - New Plant - Remove Fe/N	15,788,200	-	-	15,788,200	SPAP, City
Crosby	10	Watermain - Phase 3A Improvements	1,812,804	1,812,804	-	-	
Dassel	10	Watermain - First St. Main Replacement	818,925	818,925	-	-	
Eveleth	10	Watermain - Rosvit & Dgls Aves Water	614,924	364,924	-	250,000	IRRRB
Hanley Falls	5	Watermain - Replace	1,541,690	-	-	1,541,690	RD
Hanley Falls	5	Conservation - Replace Meters	134,000	-	-	134,000	RD
Harris	12	Source - New Well	600,000	-	-	600,000	SCDP
Lake Park	10	Treatment - Plant Rehab	1,083,625	1,083,625	-	-	
Lanesboro	10	Watermain - Repl Kirkwood St.	1,011,830	202,366	809,464	-	
Lanesboro	10	Watermain - Repl Various Streets	714,841	142,968	571,873	-	
Litchfield	7	Treatment - Rehab Plant	4,936,422	3,936,422	-	1,000,000	City
Mahnomen	10	Other - Backup Generators	220,500	-	-	220,500	RD
Mahnomen	10	Source - Upgrade Well #4	208,000	-	-	208,000	RD
Menagha	10	Storage - Repl w/100,000 Gal Tower	1,288,000	614,500	-	673,500	City
Murdock	7	Treatment - New Fe/Mn Treatment Pl	2,509,710	-	-	2,509,710	WIF/RD
Murdock	6	Storage - New 50,000 Gal Tower	896,750	-	-	896,750	RD
Perham	10	Watermain-Repl 1st Ave N, 4th & 5th S	1,832,913	1,832,913	-	-	
Pipestone	10	Other - LSL Replacement	25,000	-	12,500	12,500	City
Pipestone	10	Watermain - Replace NE Area, Ph 1	2,019,140	403,828	1,615,312	-	
Saint Paul Regional	10	Other - LSL Replacement Phase 2	500,000	-	250,000	250,000	Local
Wood Lake	13	Source - New Well #4, Seal Wells 1 &	550,000	-	-	550,000	WIF/RD
Wood Lake	12	Treatment - Repl Plant & Equipment	2,777,000	-	-	2,777,000	WIF/RD
Zimmerman	12	Source - 2 New Wells	1,136,210	1,136,210	-	-	
	24	Projects	44,378,897	13,707,898	3,259,149	27,411,850	

DWSRF = Drinking Water Revolving Fund loan (PFA)  
 DWSRF PF = Drinking Water Revolving Fund Principal Forgiveness (PFA)  
 WIF = Water Infrastructure Fund (PFA)  
 SPAP = State Special Appropriation  
 RD = USDA Rural Development  
 SCDP = Non-entitlement Community Development Block Grant  
 City or Local = Local Municipal Funds

**IV. Financial Status of the DWRF**

Table 2 (page 27) shows the sources and uses of funds in the DWRF for FY 2023, the total amounts from FY 1998 through FY 2023, and the estimated amounts for FY 2024.

The PFA has developed a financial model to estimate the average annual lending capacity of the DWRF based on the current assets in the fund. The PFA currently estimates the average DWRF lending capacity to be approximately \$58 million per year in perpetuity, assuming that federal

cap grants (Base and IJJA Supplemental) and related state match continue through FFY 2026. In many years, the PFA has used its reserves and revenue bonding authority to make loans at higher levels based on strong demand. The PFA plans to issue revenue bonds in SFY 2024 to leverage additional loan funds.

Funding demand has always exceeded annual lending capacity, which the PFA has addressed by establishing a cap on the base interest rate discount and a fundable range for new project requests based on PPL priority points. Demand for DWRf financing continues to grow, and total project requests (non-lead service line replacement projects) for the 2024 IUP are nearly \$601 million, just over 10 times the sustainable long-term lending capacity of the DWRf. To maintain balance between current demand and future lending capacity, the PFA in consultation with the MDH, each year determines a fundable range for new project on the IUP based on PPL priority points. For new projects on the 2024 IUP, the fundable range cutoff has been set at 7 points.

In approving the 2024 IUP, the PFA commits to providing DWRf loans to all Part A carryover projects and Part B new projects in the fundable range that are able to proceed within the fiscal year. The 2024 IUP includes total loan requests of \$585 million for non-lead service line replacement projects. Actual projects PFA expects to move ahead under this IUP is less, approximately \$279 million. While the total requested carryover loans exceeds the sustainable lendable capacity of the Fund, it is within a manageable level that the Fund can support in the short term. In the long term, however, without continued state support for the program, funding beyond the Fund's annual lending capacity will decrease its future lending capacity.

## **V. Set-Asides**

In addition to financing drinking water projects, the federal Safe Drinking Water Act permits states to set-aside a percentage of capitalization grant funds, including IJJA funds, for certain non-project activities, up to a maximum of 31%. States that take less than the maximum allowed amounts may choose to "bank" or "reserve" some set-asides to potentially take later from future capitalization grants, thereby maximizing the federal funds used for project loans in the short-term while preserving the ability to take a higher level of set-asides from future grants for needed set-aside activities. Table 3A identifies reserved and banked set aside funds.

Set-asides funds for the Year 2 IJJA funds and expected 2024 Base were identified in consultation with the MDH. The PFA, in consultation with the MDH, intend to use up to the percentages and amounts identified in the chart below for set-aside activities. Congress has not yet appropriated funds for the 2024 base capitalization grant so only the percentages are reflected in the chart below.

Set-Aside Funds by Capitalization Grant Type 2024 IUP											
	Program Administration		PWSS		Small System Technical Assistance		Local Assistance		Wellhead Protection		Total
	(\$)	(%)	(\$)	(%)	(\$)	(%)	(\$)	(%)	(\$)	(%)	(\$)
Base 2024*	\$ -	0%	TBD	10%	TBD	2%	\$ -	0%	TBD	10%	TBD
IJA Supplemental Year 2	\$ 1,274,000	4%	\$ 3,185,000	10%	\$ 637,000	2%	\$ -	0%	\$ 3,185,000	10%	\$ 8,281,000
IJA LSLR Year 2	\$ 1,514,760	4%	\$ -	0%	\$ 757,380	2%	\$ 3,786,900	10%	\$ -	0%	\$ 6,059,040
IJA EC Year 2	\$ 462,280	4%	\$ 231,140	2%	\$ -	0%	\$ -	0%	\$ -	0%	\$ 693,420
	\$ 3,251,040		\$ 3,416,140		\$ 1,394,380		\$ 3,786,900		\$ 3,185,000		\$ 15,033,460

\*The Base 2024 cap grant amount has not yet been allocated. The IUP identifies the MDH requested percentage/maximum percentage for the set-asides.

Set-asides taken from the Emerging Contaminants and Lead Service Line capitalization grants can only be use for activities related to emerging contaminants and lead service line activities. MDH will use Emerging Contaminant set aside funds to pay MDH staff who will work directly with water supply systems who have issues with emerging contaminants. Activities including engineering and environmental review, communications, and assistance to applicants in applying for funding. MDH will use LSL set-aside funds to pay for MDH staff working directly with LSL projects, including engineering and environmental review, communications, and assistance to applicants in applying for funding. MDH issued a Request for Proposal and developed a list of prequalified consulting engineers who can conduct LSL inventories. Public water system can apply for grants to the MDH for LSL inventory work. MDH will also provide funds to Minnesota Rural Water (sole source technical assistance provider) for a lead service line trainer (circuit rider) and funds to add LSL information to the existing University of Minnesota Infrastructure Mapping (GIS) system.

Workplans detailing set-aside activities will be prepared and submitted with the capitalization grant applications to EPA.

**VI. Transfers**

Federal regulations allow transfers up to 33% of cumulative federal capitalization grants from Drinking Water to Clean Water or vice versa. Per EPA, transfers of EC funds are based on the IJA drinking water capitalization grant allotments.

Additional time is needed to identify eligible CW emerging contaminant projects, while the MDH has identified high priority DW emerging contaminant projects on the 2024 IUP. Therefore, the PFA intends to transfer \$3,909,000 from the CW EC capitalization grant to the Drinking Water Fund to help address high priority DW EC projects on the 2024 DW IUP. PFA intends to transfer the \$3,909,000 back to the CW Fund in the future.

A transfer in the amount of \$3,909,000 will be made from the CW Fund Emerging Contaminants capitalization grant to the Drinking Water Fund for DW Emerging Contaminants projects.

## VII. Drinking Water Revolving Fund Goals

The primary objective of the DWRP is to provide loans to public water suppliers. The descending order of loan priority is to: 1) resolve infrastructure problems that pose the most serious risk to public health, 2) bring systems into compliance with drinking water requirements, and 3) assist systems in most financial need. A lower program priority is to provide suppliers with proactive assistance and support so they can operate their systems more effectively and appropriately. This assistance is accomplished through the set-aside activities of operator certification, technical assistance to small systems, capacity development, and wellhead protection. The lowest program priority is to provide loan assistance to maintain systems in a sound condition and in compliance with public water supply standards.

### *Short Term Goals:*

1. Prepare for a bond sale calendar year 2023.
2. Continue to negotiate loan amounts with applicants funded on an annual cash flow basis in order to meet project needs while limiting the annual impact on the DWRP.
3. Continue to promote asset management for DWRP recipients.
4. Utilize set-asides to provide technical assistance for LSLR projects and conduct RFP for LSLR inventory work (MDH).
5. Actively coordinate DWRP loans with other PFA funding, including state Water Infrastructure Funds (WIF) grants and other state and federal agency programs to maximize the number of projects funded on the Project Priority List.
6. Coordinate Emerging Contaminants projects for small and disadvantaged communities with the Department of Health's Small Underserved and Disadvantaged Community (SUDC) grant funding.
7. Coordinate the State's Lead Service Line Replacement Grant Program with the IJJA Lead Service Line Replacement funds.
8. Coordinated emerging contaminants projects with the MDH's Small Underserved and Disadvantaged Communities (SUDC) grant funds.

### *Long Term Goals:*

1. Provide financial and other assistance (including the set-aside activities) to public water supply systems in order to protect the public health and achieve and maintain compliance with the Safe Drinking Water Act, while following sound lending practices.
2. To the maximum extent possible, provide timely funding for all projects that receive technical approval and certification from the MDH, including projects eligible for principal forgiveness and WIF.
3. Leverage the capitalization grants as appropriate in order to finance as many projects as possible while maintaining sufficient cash flows to meet future project needs.



4. Manage the assets of the Fund in perpetuity so that it is a permanent resource to assist public water systems in the State.
5. To implement technological solutions to increase efficiencies with program operations.
6. To make funds available to as many high-priority projects as possible while maintaining a steady and sustainable fundable range.

*Set-Aside Goals:*

1. Public Water System Program Administration. Maintain an up-to-date, statewide public water system program that consists of providing technical expertise. establishing standards, monitoring, education, enforcement and public information.
2. Technical Assistance to Small Systems. Provide personal, non-regulatory technical assistance to water supply operators so they can effectively manage the complexities of the systems they operation, and for operators whose systems utilize groundwater, to also identify and manage potential sources of contamination, including LSLR activities.
3. Wellhead Protection. To implement Minnesota's EPA approved wellhead protection program in order to effectively manage potential contaminant sources in the areas that contribute water to wells.
4. Implement the Lead Service Line Technical Assistance Master Contract and Inventory activities.

### **VIII. Cross-Collateralization**

As permitted by Congress in legislation approved in 1997, the PFA has cross-collateralized the bonds sold for the DWRP and the Clean Water Revolving Fund. The purpose is to enhance the security of bonds sold for both programs, thereby improving the credit rating and reducing the interest rate on the bonds. This allows the PFA to pass on the best possible interest rates to its borrowers. The revenues from loan repayments in each program are pledged first to the bonds for that program. After the revenues in each program have been used to make the PFA's bond debt service payments and meet all other payment and coverage requirements under the bond resolutions, funds in excess of these requirements may be used to cover a default in the other program.

Given the coverage requirements the PFA must meet for its bonds, the general obligation pledges provided by the borrowers, and the financial management practices of the PFA (as reflected by the AAA rating of its bonds), it is very unlikely that a default would occur. The cross-collateralization of the two programs will, however, provide even more assurance to the bondholders and enhance the financial strength of the programs.

**IX. Tables and Appendix**

Table 1: 2024 Intended Use Plan Project List (pages 18-26)

Table 2: Sources and Uses of Funds (page 27)

Table 3: Set-Asides Reserved/Banked (page 30)

Appendix: Minnesota Department of Health 2024 Project Priority List

**X. Websites for Further Information**

Minnesota Public Facilities Authority:

[www.mn.gov/pfa](http://www.mn.gov/pfa)

Minnesota Department of Health:

[www.health.state.mn.us/divs/eh/water/dwrf/index.html](http://www.health.state.mn.us/divs/eh/water/dwrf/index.html)

**XI. Questions and Comments**

Questions or comments regarding the 2024 IUP should be directed to:

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