



## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

The National Rural Electric Cooperative Association (NRECA) is the national service organization dedicated to representing the national interests of cooperative electric utilities and the consumers they serve. NRECA is the national service organization for more than 900 not-for-profit rural electric utilities that provide electric energy to over 42 million people in 47 states or 12 percent of electric customers. Kilowatt-hour sales by rural electric cooperatives account for approximately 11 percent of all electric energy sold in the United States. NRECA members generate approximately 50 percent of the electric energy they sell and purchase the remaining 50 percent from non-NRECA members. The vast majority of NRECA members are not-for-profit, consumer-owned cooperatives. NRECA's members also include approximately 67 generation and transmission ("G&T") cooperatives, which generate and transmit power to 668 of the 838 distribution cooperatives. The G&Ts are owned by the distribution cooperatives they serve. Remaining distribution cooperatives receive power directly from other generation sources within the electric utility sector. Both distribution and G&T cooperatives were formed to provide reliable electric service to their owner-members at the lowest reasonable cost.

NRECA appreciates RUS's efforts to make its loan requirements more transparent. This new Rural Determination rule addresses one of the most fundamental aspects of the RUS program – the scope of RUS's lending authority. This rule needs to be carefully crafted to ensure that RUS is fully and appropriately utilizing its lending authority. As evidenced by the length of this submission, our members, who know the RUS electric loan programs better than any other group of participants in the electric industry, have a large number of questions and concerns. NRECA requests that RUS carefully consider these and other comments RUS receives, and before issuing a final rule, issue a revised proposed rule and provide another opportunity for public comment. We believe this will improve the clarity and effect of the final rule, which will allow RUS to operate more efficiently and effectively.

**The proposed rule appears to expand RUS's lending authority beyond the authority granted in the Rural Electrification Act (REAct).** Part 1710.104 (b) as proposed in the rule would provide that loans may be approved for facilities that serve non-REAct beneficiaries only if:

- The primary purpose of the loan is to furnish or improve service for REAct beneficiaries and the use of loan funds to serve non-REAct beneficiaries is necessary and incidental to the primary purpose of the loan; **or**
- The requirements of 1710.116 and 1710.117 are satisfied.

Similarly, the second sentence of proposed Part 1710.116 (a) states: "Borrowers serving, directly or indirectly, any person located within a rural area shall be considered eligible for financing as provided in this section and §1710.117." and proposed Part 1710.151(e) states:

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

“Whenever a borrower proposes to use loan funds for the improvement, expansion, construction, or acquisition of electric projects for non-REAct beneficiaries, there is satisfactory evidence that such funds are necessary and incidental to furnishing or improving electric service for REAct beneficiaries (see Part 1710.104) or the requirements of Part 1710.116 and 1710.117 are satisfied.”

These proposed changes all appear to allow RUS to make loans even if the loan is not for the primary purpose of serving REAct beneficiaries. RUS’s regulations currently in Parts 1710.104(b) and 1701.151(e) reflect RUS’s long-standing interpretation of the scope of its lending authority under the REAct as being limited to providing and improving electric facilities that serve non-REAct beneficiaries only if the primary purpose of the loan is to furnish or improve service for REAct beneficiaries. Other than the limited exception in Section 317 of the REAct for loans for electric generation from renewable energy resources for resale to rural and non-rural residents, nothing in the REAct can reasonably be interpreted to allow RUS to expand its lending to include loans for purposes that are not primarily intended to furnish or improve service in rural areas.

The changes proposed to Parts 1710.104(b) and 1701.151(e) should not be made, and the second sentence of proposed new Part 1701.116(a) should be deleted. Instead RUS should clarify that Parts 1710.116 and 1710.117 are designed to clarify, in circumstances where a significant portion of a project will serve non-rural consumers, that RUS may finance a share of the costs of the total project that is proportionate to the percentage of rural area that will be served from the project, thus ensuring that the primary purpose of RUS’s loan is to serve rural areas and service to non-rural areas is necessary and incidental to furnishing or improving electric service for REAct beneficiaries.

**The proposed rule does not appropriately implement the preference for not-for-profit borrowers required by the REAct. In any fiscal year RUS should process loan applications for all types of projects (generation, transmission, distribution, energy efficiency) from all non-profit borrowers before processing any loan applications for for-profit borrowers.**

- The REAct mandates that RUS give preference to “States, Territories, and subdivisions and agencies thereof, municipalities, people’s utility districts, and cooperative, nonprofit or limited-dividend associations”. 7 USC § 904(a) (2009). Nothing in Section 317 or any other section of the REAct changes this basic preference. Therefore, in implementing all of its financing authority, including authority under Section 317, RUS must give preference to not-for-profit electric cooperatives and these other governmental entities.
- The special limitations on the amount of loans to be made to for-profit utilities are not sufficient to implement the preference for non-profit and governmental borrowers required by the REAct. Limiting the amount of any one loan to for-profit borrowers still leaves open the possibility that for-profit entities use up most or all of RUS’s

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

appropriations in any given fiscal year. Instead, RUS should process all applications from REAct preference applicants first.

- In addition, the proposed rule sets forth limitations for loans to for-profit entities for generation assets, but does not apply any special limitations on Financing Percentage for for-profit utilities for loans for transmission, distribution or energy efficiency projects. Consistent with the REAct's preference for loans to not-for-profit and governmental entities, the same limitations should apply to loans to for-profit borrowers for transmission, distribution, or energy efficiency projects.
- The proposed rule should be clarified such that any special limitations on loans to for-profit entities do not apply to affiliates of a not-for-profit entity if the not-for-profit entity is the offtaker of 100% of the generation, transmission, distribution or energy efficiency services to be provided by the affiliate. Not-for-profit entities may own projects through taxable affiliates that are not organized as not-for-profit cooperatives to allow the not-for-profit entity to benefit from tax incentives, or for other reasons.

**The proposed rule should be modified to clarify that all borrowers, whether under Section 317 and whether for-profit or not-for-profit, will be subject to RUS regulations and loan and mortgage requirements in the same way that RUS borrowers have been in the past.** RUS has successfully supported the electrification of the rural United States using a system-wide lien finance structure under which borrowers that are load serving utilities pledge their entire electric systems as security. System financing has resulted in excellent performance of the RUS loan portfolio for both taxpayers and borrowers. The default rate for the REAct electric loan and loan guarantee programs is less than 1%. Default rates and losses due to default since the inception of the REAct program in 1936 have been extremely low. By making its rural determination rules more transparent, RUS may attract new applicants that would prefer different loan structures. RUS does not have sufficient staff to create different loan requirements for new types of borrowers.

**RUS's proposal in Part 1710.119 to give priority to loans for renewable generation facilities or transmission facilities that deliver renewable energy could be counterproductive to RUS's core mission.** Under RUS's current regulations, priority is given to loans for restoring service after a major catastrophe, bringing existing facilities into compliance with new environmental laws, financing capital needs resulting from a merger or acquisition of another electric system or to correct safety problems. These types of activities all support the fundamental financial and operational health of a borrower, by allowing it to recover from a catastrophe, protect the value of substantial investment in generation assets that must be upgraded to comply with new laws, benefit from economies of scale through merger or acquisition of another system or maintain basic safety standards. Renewable energy projects are not intrinsically fundamental to a borrower's financial or operational health in the same way.

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

RUS should continue to focus its efforts on its core mission of furnishing and improving electric service in rural areas. Availability of reliable, reasonably priced power has proven time and again, in the United States and throughout the world, to be the backbone of economic growth and development. For any particular borrower at any particular time, the best way to do that may or may not include renewable generation or transmission for renewable generation. To the extent that loan requests exceed available appropriations, RUS should give priority to loans that will best serve its core mission.

**The proposed rules appear to expand the scope of service area that is considered rural under the REAct for borrowers that had outstanding loans or loan guarantees on June 18, 2008.** RUS correctly notes in the preamble to the proposed rule that under the current definition of rural area in the REAct, it is the service territory of a borrower that had an outstanding RUS loan on June 18, 2008 that is grandfathered as “rural”, and not the borrower itself. However, as drafted, the proposed rule appears to treat the entire service territory of a borrower that had an outstanding RUS loan on June 18, 2008 as “rural” in some instances.

- Part 1710.117 (c) states: “The Financing Percentage for June 2008 Borrowers shall be 100 percent limited only by an underwriting requirement as may be determined by RUS pursuant to paragraph (b) of this section.” In contrast, Rural Percentage is fixed at 100 percent only for June 2008 Borrowers that have not acquired new service territory since June 18, 2008. To be consistent with the definition of rural in the REAct, this same qualification regarding no acquisition of new service territory should be applied to this rule fixing the Financing Percentage of June 2008 Borrowers at 100%.
- A similar fix needs to be made to Part 1701.117 (d), which states: “The percentage of generation capacity or energy financed in all or part by RUS for utility systems other than June 2008 Borrowers many not exceed the Rural Cap.”
- Part 1701.117(e)(1) states that “June 2008 Borrowers may seek financing for 100 percent for a transmission investment only in [certain cases].” This should be modified to provide that RUS can provide up to 100% financing for June 2008 Borrowers that have not acquired new service territory since June 18, 2008.

**The proposed rule does not clearly state, as RUS correctly did in the preamble, that only non-rural areas located within the additional service area acquired by a June 2008 Borrower after June 18, 2008 will reduce a June 2008 Borrower’s Rural Percentage below 100%.** Part 1701.116 of the proposed rule should be modified to incorporate this principle.

**Appropriations and credit subsidy calculations for loans to entities that are not entitled to preference under the REAct should be separate from appropriations and credit subsidy calculations for REAct preference borrowers.** The vast majority of RUS borrowers to date have been REAct preference borrowers, most of whom are not-for-profit electric cooperatives. The not-for-profit electric cooperative business model is a low risk model, and the RUS loan

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

program has enjoyed over 76 years of tremendous success, with extremely low default rates. In recent years, REAct loans and guarantees have been charged little or no credit subsidy, and at times have received a negative credit subsidy, under the Federal Credit Reform Act. It appears that RUS may be intending to attract more non-REAct preference borrowers by making its rules regarding the limits of its lending authority clear. NRECA is supportive of RUS continuing to support rural electrification, as long as in doing so RUS does not erode its ability to continue to support its existing borrowers, who serve the vast majority of the rural United States.

Appropriations and the credit subsidy for new borrowers that are not electric cooperatives and have a credit profile that is not as strong as the typical electric cooperative should be done separately, so that higher credit risk borrowers do not erode the amount of appropriations available for lending to lower credit risk borrowers.

**RUS and its borrowers will benefit if RUS delays making any changes to Parts 1710.253 and 1710.254 until RUS has completed its streamlining project and is ready to modify these and other provisions of its regulations to implement its streamlining efforts.** The changes proposed to these two sections are not necessary in connection with RUS's adoption of a formal regulation regarding rural determinations and related limitations on the availability of RUS financing. In any event, any exceptions from certain RUS rules for renewable generation proposed to meet RPS requirements should be more limited. The changes proposed to Part 1710.253 would eliminate any requirement that engineering and cost studies for generation using renewable fuel proposed to meet a renewable portfolio standard include consideration of system reliability, alternative unit sizes or alternative types of generation. While the need to meet a renewable portfolio standard limits a borrower's choice of generation by excluding generation fueled by non-renewable fuels, there can be more than one type of renewable generation facility (hydro, solar, wind, geothermal, biomass) available to a borrower. There is no reason why a borrower should not consider the potential effect on system reliability of different types of renewable generation available to it, or evaluate different unit sizes of available renewable energy technologies or alternative types of renewable generation when adding generation to its system to comply with a renewable portfolio standard. Rather than eliminating consideration of these factors, consideration of these factors should be narrowed to include only the types of renewable generation facilities that are practical for the borrower. For example, wind generation is not currently considered a viable option in most of the southeastern United States, and geothermal generation is generally considered commercially viable only on a large scale in very limited geographic regions of the United States.

Similarly, the proposed change to Part 1710.254 would deem that all the requirements of Part 1710.254 for evaluation of alternative sources of power would be met if the proposed generation project is a renewable energy project proposed to meet a renewable portfolio standard. Again, while the need to meet a renewable portfolio standard limits a borrower's choice of generation by excluding generation fueled by non-renewable fuels, there can be more than one type of renewable generation facility (hydro, solar, wind, geothermal, biomass) available to a borrower. Further, under most RPS requirements, utilities can meet the RPS requirements by self-generating renewable energy, or purchasing renewable energy from generation facilities owned

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

by others. There is no reason to abandon a prudency review of a borrower's decision to build its own renewable generator, rather than purchase renewable energy from a third party

\* \* \*

**In addition to the broader issues described above, NRECA has specific comments and questions regarding a number of aspects of the proposed rule.**

### **1710.2 – Definitions**

- June 2008 Borrower – This definition should be modified to clarify that June 2008 Borrowers include entities that had outstanding loans that were guaranteed by RUS, and not only entities that had direct loans from RUS.
- Sponsoring Utility – It is not clear what RUS is attempting to do by limiting loans where the borrower is an owner of the proposed transmission facility, but is not obligated under an “offtake agreement”. The term offtake agreement needs to be defined, or the concept of Sponsoring Utility needs to be further explained, so that the proposed rule can be evaluated and commented on.
- Utility – The requirement that the entity have a “published tariff that the entity and any associated regulatory agency may adjust” would eliminate many G&T power supply borrowers from being eligible to be a “Sponsoring Utility”. Many G&T power supply borrowers are not regulated by a state regulatory agency or FERC, and thus do not have a published tariff. It is not clear why RUS believes this requirement is important.

### **1710.101 – Types of eligible borrowers**

- This proposed change deletes the two final sentences of Part 1701.101(f), which is an appropriate change, given the new regulations being proposed for determining Rural Percentage. However, without these two sentences, the meaning of the remaining sentence becomes less clear. In particular, the reference to “REAct beneficiary loads accruing from the time the former borrower's loan application is received by RUS” is unclear, and could be read to refer only to load added by the borrower after its new loan application is received by RUS. This statement would be clearer if the words “accruing from the time” were changed to “determined as of the time”.

### **170.116 – Rural Determination**

- Subsection (d) provides that the “Rural Percentage” for a June 2008 Borrower that has “not acquired any new service territory since June 18, 2008” is 100%.

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

- In the preamble commentary to the proposed rule, RUS states that existing borrowers as of June 18, 2008 “which have not since experienced any growth in their service areas via acquisition or merger are 100 percent rural.”
- Consistent with its statements in the preamble commentary, RUS should clarify the meaning of “acquired new service territory” to refer to acquisitions of territorial service rights or customers from another utility, and not to include addition of new customers to the borrower’s system pursuant to rights which the borrower had under applicable state laws as of June 18, 2008 to provide retail electric service in a geographic area or to a type of customer.
- Further, this rule should also clarify that a merger or acquisition of territory between two June 2008 borrowers does not constitute an acquisition of new service territory unless the combined service territory of the surviving June 2008 borrower includes service territory that neither one of the two June 2008 borrowers had as of June 18, 2008.
- This subsection also needs to clarify how RUS will determine:
  - What the service territory of a power supply borrower (and any other borrower that does not provide retail electric service) was as of June 18, 2008. This should be defined as the combined service territory of all of the borrower’s members as of June 18, 2008, regardless of whether the member was an RUS borrower as of June 18, 2008; and
  - Whether a power supply borrower (and any other borrower that does not provide retail electric service) has “acquired new service territory” since June 18, 2008. This should be determined on the basis of whether the power supply borrower’s members have acquired new service territory (as described above).
- Subsection (f) establishes four methods for determining the “Rural Percentage” of service territory of any borrower that was not a borrower as of June 18, 2008 and any borrower that was a borrower as of June 18, 2008 that has acquired new service territory since June 18, 2008. The fourth method applies only to generation projects of 50 MW or less that are either (1) located in a rural area at least 10 miles from an urban area or (2) located in an urban area and can clearly demonstrate benefit for a rural area. Rural Percentage for these projects is to be determined first by identifying from load flow studies the geographic boundaries of where power from the facility will flow during low consumer demand, and then applying one of the 3 determination methods above to determine the percentage of the area within that boundary that is rural.

# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

- NRECA does not understand why this method is needed, or why it would be applicable only to projects of 50 MW or less located in certain described areas. RUS's lending authority is defined by the purpose of the loan, not the location or size of the assets being acquired with the proceeds of the loan. In addition, the load flow analysis described in the rule is not an analysis that is routinely done, so at a minimum RUS would need to provide more guidance as to how such load flow studies should be performed. Perhaps RUS is contemplating applying this method to special purpose entities that are developing new generation projects, and don't have a defined retail service territory. In such a case, it would be more appropriate for RUS to determine the Rural Percentage by evaluating the Rural Percentage of the entity(ies) that will be purchasing power from the facility.

### **1710.117 – Financing Percentage**

- Subsection (e) regarding transmission loans:
  - Method T1 needs to be modified to provide that June 2008 Borrowers that have not acquired new service territory since June 18, 2008 can obtain 100% RUS financing.
  - The term “integrated transmission system” needs to be defined. It should include transmission systems operated by an RTO or ISO in which the applicant's transmission facilities are operated by the RTO or ISO, and contractual arrangements among transmission owners for joint operation and use of each other's interconnected transmission facilities.
  - The proposed rule in this Part 1710.117 (e) refers to “existing borrowers” several times. It is not clear why - there is no basis other than 7 U.S.C. § 913 for distinguishing between existing borrowers and new applicants.
  - The proposed rule does not indicate how RUS will address a loan for a June 2008 Borrower that does not meet one of the three criteria set forth under Method T1.
  - The proposed rule needs to define what projects are considered “transmission” and what projects are considered “distribution”. Further, the proposed rule should be clarified to provide that stand-by generators and other generation equipment that is intended for use for transmission reliability or stability should be addressed as “transmission” and not as “generation”.
- Subsection (g) regarding energy efficiency projects only permits RUS to loan for energy efficiency projects located in rural areas.



# NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

## **Comments on RUS Notice of Proposed Rulemaking on Rural Determination and Financing Percentage**

- Energy efficiency can have long term benefits for load serving entities by slowing load growth and thus extending the amount of time before the load serving entity will need to obtain additional capacity and/or energy. Thus, RUS should support energy efficiency based on the borrower's Rural Percentage, just as it does for generation, transmission and distribution.
- At a minimum, this should be changed to provide that RUS will loan 100% for energy efficiency projects for any June 2008 Borrower that has not acquired new service territory since June 18, 2008.

### **1710.251 – Construction work plans – distribution borrowers**

- This rule addresses the types of project that a distribution borrower may include in a construction work plan. Under the current rule, borrowers may include “communications equipment and meters” in their construction work plans. The proposed rule would limit this category to “smart grid facilities including communications equipment, smart meters, load management equipment, automatic sectionalizing facilities, and centralized System Control and Data Acquisition equipment.” It would further limit financing for “load management equipment and other smart devices” to “capital equipment designed to influence the time and manner of consumer use of electricity, which includes peak clipping and load shifting” so long as such equipment is owned by the borrower.
- RUS has not provided any explanation of the changes it is intending to make with this new rule, or the reasons for those changes. It appears to eliminate financing eligibility for any meters that are not “smart”, regardless of whether installation of “smart” meters on a borrower's system is a prudent financial or operational decision. The rule does not define what “smart” means.

### **1710.252 – Construction work plans – power supply borrowers**

- The change to subsection (c)(2) of this rule appears to expand the types of facilities to be included in a power supply borrower's construction work plan. The current rule refers to “Systems Control and Data Acquisition equipment, including communications, dispatching and sectionalizing equipment, and load management equipment. The proposed rule adds “smart grid facilities such as” to the beginning of this list.
- Again, RUS has not provided an explanation of this change, or the reasons for it. It is unclear why RUS appears to be expanding the types of equipment eligible for inclusion in a power supply borrower's work plan to include “smart grid” equipment, but at the same time limiting eligible equipment for distribution borrowers to only “smart” equipment.

**NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION**

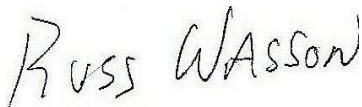
**Comments on RUS Notice of Proposed Rulemaking  
on  
Rural Determination and Financing Percentage**

- The change to subsection (c)(4) of this rule adds “including generation facilities that use renewable fuel” as a non-exclusive list of the kinds of “improvements and replacements of generation facilities” that are to be included in a construction work plan. The addition of this language does not appear to change the substance of what is required to be included in a construction work plan. RUS has not provided an explanation of this change.

\* \* \*

NRECA recognizes that writing a rule to comprehensively address how RUS will determine the scope of its lending authority in a myriad of circumstances is a complex task. We reviewed the rule carefully, and have attempted in these comments to identify at a high level our concerns and questions. We expect that RUS may have questions about these comments, and comments it receives from others, given the breadth and complexity of issues the proposed rule addresses. Again, we encourage RUS to consider these and other comments RUS receives, and before issuing a final rule, issue a revised proposed rule and provide another opportunity for public comment. We believe this will improve the clarity and effect of the final rule, which will allow RUS to operate more efficiently and effectively.

Respectfully submitted,



---

Russell Wasson  
Director Tax, Finance & Accounting Policy  
National Rural Electric Cooperative Association  
[Russell.Wasson@nreca.coop](mailto:Russell.Wasson@nreca.coop)  
Ph: (703) 907-5802