

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 1		[12/31/2020] – Review Date



## Drinking Water State Revolving Loan Fund – Loan Management Policies

*These Policies are adopted on [June 27, 2019] by the Board of Directors of the New Mexico Finance Authority (“Finance Authority” or “NMFA”), a public body politic and corporate, separate and apart from the State of New Mexico constituting a governmental instrumentality, created by the New Mexico Finance Authority Act, Section 6-21-1 et. seq., NMSA 1978.*

### I. PURPOSE

#### A. Purpose Statement

The New Mexico Drinking Water State Revolving Loan Fund Act (the “Act”) was created to provide local authorities with low-cost financial assistance in the construction and rehabilitation of necessary drinking water facilities through the creation of a self-sustaining revolving loan program so as to improve and protect drinking water quality and public health. Pursuant to the Act, NMFA is partnered with the New Mexico Environment Department (“NMED”) in the operation of the Drinking Water State Revolving Loan Fund (“DWSRLF”). These Loan Management Policies set forth the criteria by which the NMFA may make DWSRLF loans to qualified entities.

#### B. Objectives

The goal of these Loan Management Policies is to provide guidance to NMFA staff and borrowers regarding acceptable levels of risk, pricing and securitization of individual loans, and structuring enhancements within the DWSRLF program.

#### C. Implementation

These Loan Management Policies shall be implemented by the New Mexico Finance Authority Board and may, at times, be waived by the Board if the Board determines that a deviation from its adopted policies is necessary. Such waiver will be reflected in the minutes

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 2		[12/31/2020] – Review Date

of the meeting at which the waiver is considered and must not conflict with federal regulations and the approved State’s Environmental Review Process document.

## II. DEFINITIONS

- A. **“Additional Bonds Test”** – Calculation to determine if a borrower’s revenues meet levels required by the NMFA to incur additional debt against a financed facility.
- B. **“Additional Subsidy”**– Principal Forgiveness provided under the DWSRLF program and as allowed under state law.
- C. **“Capitalization Grant”** – An award of funds by the United States Environmental Protection Agency (EPA) to a State for the purpose of capitalizing and administering the DWSRLF, as authorized in Section 1452 of the Safe Drinking Water Act.
- D. **“Comprehensive Priority List”** – The list of prioritized water system projects using the criteria enacted by the NMED and listed in the Intended Use Plan.
- E. **“Cost of Issuance”** – A 1% fee added to loan draws to cover the cost of legal services, construction monitoring, and engineering and environmental review; Cost of Issuance is not charged to entities qualifying as Severely Disadvantaged.
- F. **“Disadvantaged Entities”**– An applicant whose MHI is greater than 80% but less than 100% of the State’s MHI, based on the most recent 5-year average of MHI from census data or through a survey acceptable to NMFA.
- G. **“EPA”** – United States Environmental Protection Agency.
- H. **“EPA equivalency”** – The total dollar amount of projects funded by the Capitalization Grant that meet specific federal requirements.
- I. **“Federal Regulations”** – The collection of rules under which the DWSRLF is governed. Specifically, these include but are not limited to, 40 CFR 9 and 35, the Interim Final Rule, and the Safe Drinking Water Act, Section 1452.
- J. **“Financial Capacity”** – A water system’s ability to maintain sufficient financial resources to allow the system to maintain compliance with federal and state laws.

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 3		[12/31/2020] – Review Date

- K. **“Fundable Priority List”** – The list of projects appearing on the Comprehensive Priority List that have demonstrated Technical Capacity, Managerial Capacity, and Financial Capacity and are ready to proceed.
- L. **“Green Projects”** – Means green infrastructure, water conservation, energy efficiency improvements, or other environmentally innovative activities.
- M. **“Intended Use Plan” or “IUP”** – The annual document prepared by both the NMED and NMFA which identifies the intended uses of the Capitalization Grant, and describes how those uses support the overall goals of the program.
- N. **“Interim Period”** – The construction period of a DWSRLF loan during which only interest and fees are charged to the borrower on requisitioned amounts.
- O. **“Maximum Annual Debt Service” or “MADS”** – The amount of debt service for the year in which the greatest amount of debt service payments are required.
- P. **“Managerial Capacity”** – A water system’s ability to maintain system operations, as determined by NMED.
- Q. **“Median Household Income”** – The median of the combined incomes for persons living within one household, used by the NMFA to determine if a community qualifies as Disadvantaged under this Policy.
- R. **“Minimum Coverage Requirement”** – The minimum ratio of revenue available to service the debt-to-debt service required on a loan.
- S. **“Parity Lien”** – A lien with the same priority for payment from Pledged Revenues or other security.
- T. **“Pledged Revenue”** – The revenue generated by the borrower pledged to the NMFA from which the borrower will fund repayment of the loan.
- U. **“Principal Forgiveness”** – Same as **“Subsidy;”** the amount of principal that does not require repayment.
- V. **“Regionalized Community”** – The residents of an area benefiting from the water system improvements to be financed with the proceeds of the grant or loan.

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 4		[12/31/2020] – Review Date

- W. **“Senior Lien”** – Lien with higher priority for payment from Pledged Revenues or other security.
- X. **“Severely Disadvantaged Entities”** – An applicant with an MHI 80% or less of the State’s MHI, based on the most recent 5-year average of MHI from census data or through a survey acceptable to NMFA.
- Y. **“State Environmental Review Process” or “SERP”** – The necessary components of an environmental information document prepared by the applicant, and the steps necessary for NMFA to make a determination regarding any potential environmental impacts of a proposed project.
- Z. **“Technical Capacity”** – The adequacy of operation, and physical infrastructure of a water system, including the water source, treatment, storage and distribution system, which allows the public water system to achieve and maintain compliance with federal and state laws.

### III. ROLES AND RESPONSIBILITIES

- A. New Mexico Environment Department’s Drinking Water Bureau is responsible for the determination and promulgation of a Fundable Priority List that:
  - 1. Meets the federal regulations.
  - 2. Gives priorities to projects that cure imminent health and safety concerns.
  - 3. Designates projects that qualify as Green Projects.
- B. Water Resources Staff shall be responsible for:
  - 1. Coordinating with the Applicants appearing on the Fundable Priority List to complete and submit applications for financial assistance from the DWSRLF.
  - 2. Determining an Applicant’s Disadvantaged Entity status.
  - 3. Determining the amount of additional subsidy, if any, that an applicant is eligible to receive pursuant to these Loan Management Policies.
  - 4. Determining a project’s compliance with the SERP and federal conditions.

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 5		[12/31/2020] – Review Date

5. Determining borrower concentration within the DWSRLF loan portfolio.
  6. Monitoring project construction and compliance with applicable federal regulations.
- C. Public Lending Department Staff shall be responsible for:
1. Underwriting, structuring and presenting for approval DWSRLF loans that meet the Minimum Coverage Requirements and Additional Bonds Test requirements outlined in these policies.
  2. Administration and monitoring of permanent DWSRLF loans.

#### IV. GENERAL CONSIDERATIONS

- A. Project Eligibility. Each project funded by the DWSRLF must meet the following federal regulations.
1. Projects funded by the DWSRLF must demonstrate Technical Capacity, Managerial Capacity and Financial Capacity to undertake the proposed water project and must appear on the Fundable Priority List.
  2. Compliance with the State Environmental Review Process: Projects funded with DWSRLF funds may be used only for a project whose environmental effects were assessed pursuant to NMFA’s State Environmental Review Process approved by the EPA. This review process ensures that adequate notice to the public has been made regarding the environmental findings prior to providing financing.
  3. Loans will not be made until after NMFA has published its environmental determinations and adequate notice has been provided to the public.
- B. Green Project Reserve: Consistent with the goals of the EPA, the NMFA and NMED may set-aside portions of its loan funds for projects that qualify as Green Projects.
- C. Concentration: The NMFA will limit the DWSRLF funds so that no single borrower comprises more than 20% of the loan fund portfolio.

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 6		[12/31/2020] – Review Date

**D. Cost of Issuance:** In order to satisfy legal services, construction monitoring, and engineering and environmental review associated with the DWSRLF loans, the NMFA will incorporate into the principal amount of the loan a cost of issuance fee totaling 1% of the project costs, which will be collected on a per-draw basis, to the extent permitted by federal regulations. In accordance with federal regulations, fees collected will be held outside of the DWSRLF and used only for purposes allowed by law.

**V. LOAN STRUCTURING AND RISK MITIGATION**

**A. Loan Structure:** All DWSRLF loans will be structured with an Interim Period for a period of up to two years during which only interest and administrative fees will be paid on the amounts drawn.

1. Following the expiration of the Interim Period, or the certification of the last draw, whichever comes first, the loan will be converted to a permanent loan and a final debt service schedule will be provided to the borrower. The loan conversion to a permanent loan must occur within one year of initiation of the system’s operation.
2. The permanent loan will be structured with an amortization of up to 30 years payable monthly.
3. The NMFA Board may approve a loan to have a longer Interim Period if the project’s construction estimates indicate a longer construction phase is necessary. This approval will be noted in the NMFA Board minutes at which the loan is approved.
4. All DWSRLF loans shall be pre-payable by the borrower at the conclusion of the interim period without penalty.

**B.** In order to mitigate risk in the DWSRLF while maintaining a diverse pool of borrowers, the NMFA will take the following steps in structuring a transaction:

1. Lien: Generally, NMFA secures its loans on a Parity Lien with any other lenders. The NMFA may agree to accept a security pledge that is subordinate

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 7		[12/31/2020] – Review Date

to the payment of another lender if the identified Pledged Revenue has a strong, positive historical trend and the overall coverage adheres to the Minimum Coverage Requirements and Additional Bonds Test requirements.

2. Loan Repayment: Monthly receipt of loan payments from borrowers provides the NMFA with early indication of potential loan defaults. Generally, when a monthly revenue stream is available, the NMFA will require its loans to be paid monthly. The NMFA may allow borrowers to pay semi-annually; provided, the requesting entity has demonstrated ability to meet prior debt obligations and has sufficient staffing to manage timely loan payments.
3. All loans will be structured utilizing an executed intercept agreement if the NMFA is statutorily allowed to intercept the Pledged Revenue. The NMFA may agree to hold an executed intercept agreement in abeyance while the borrower makes monthly principal and interest payments on its loan under the following conditions:
  - a. If the borrower fails to make the agreed upon payments in a timely manner, the NMFA will immediately begin to intercept the Pledged Revenues pursuant to the intercept agreement for the duration of the loan.
  - b. This “contingent” or “suspended” intercept arrangement may be offered only to borrowers that have demonstrated ability to meet prior debt obligations and have sufficient staffing to manage timely loan payments.

## VI. DISADVANTAGED COMMUNITY ASSISTANCE AND ADDITIONAL SUBSIDY

- A. Affordability Criteria. Capitalization Grant recipients are required to define Affordability Criteria and to provide additional assistance to Disadvantaged Communities. Pursuant to public comment, NMFA defines affordability based upon MHI of the applicant and provides for two levels of Disadvantaged entity status:

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 8		[12/31/2020] – Review Date

1. Disadvantaged Entities – to be considered a Disadvantaged entity, the applicant’s MHI must be greater than 80% but less than 100% of the State’s MHI, based on the most recent 5-year average of MHI from census data or through a survey acceptable to NMFA.
  2. Severely Disadvantaged Entities - to be considered a Severely Disadvantaged entity, the applicant’s MHI must be 80% or less of the State’s MHI, based on the most recent 5-year average of MHI from census data or through a survey acceptable to NMFA.
  3. Applications for Regionalization projects may use the MHI of the community proposed for incorporation into the applicant’s water system service area for purposes of determining Disadvantaged entity status. These applications will be limited in scope to project elements related to the provision of water to the Regionalized Community and all assets funded by the loan must be owned and maintained by the borrower.
- B. Disadvantaged Community Assistance.** Capitalization Grant recipients are required to provide additional subsidy to its borrowers. NMFA provides additional subsidy in the form of loans with principal forgiveness, with the percentage of the principal forgiven determined by the NMFA Board of Directors at loan approval. The principal not forgiven will be structured and priced as provided otherwise in these Loan Management Policies.
- C.** The amount of additional subsidy provided will be promulgated each year in the State’s Intended Use Plan and is subject to federal appropriation. Pursuant to CFR §35.3525(b), DWSRLF capitalization grant recipients must provide at least 6% but no more than 35% of the capitalization grant amount for additional subsidy for state-defined Disadvantaged Communities. From time to time, Congress may require capitalization grant recipients to provide additional subsidy to its loan recipients.
- D.** No single applicant may receive more than 50% of the total additional subsidy available for disadvantaged communities in any given year. Any additional funds required to complete the proposed project will be financed at the terms offered



Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 9		[12/31/2020] – Review Date

to non-disadvantaged communities. This limitation may be waived if there is not sufficient ready demand among disadvantaged communities.

**E. Determination of additional subsidy:** The NMFA will provide additional subsidization in the form of principal forgiveness for projects using the following guidelines:

4. Borrowers subject to federal construction requirements (Davis Bacon Wage Act, American Iron and Steel, etc.) will be offered a 25% subsidy. Loans for Planning and Design only will not receive this subsidy.
5. NMFA will provide additional subsidy to Disadvantaged Entities who meet affordability criteria based on the Median Household Income (MHI) of the applicant. NMFA provides two levels of disadvantaged entity status:
  - a. Disadvantaged Entities are provided 25% principal forgiveness;
  - b. Severely Disadvantaged Entities are provided with an additional 25% principal forgiveness and will not be charged a 1% Cost of Issuance fee; and
6. Certified “Green Projects” will be provided with an additional 25% of principal forgiveness.
7. No project shall receive more than 75% in total principal forgiveness.
8. Private non-profit and private for-profit systems are not eligible for subsidy due to the New Mexico anti-donation clause (Art IX, Sec. 14).

## VII. INTEREST RATES

- A.** To help offset costs associated with federal loan program compliance and to provide incentive for a system to undertake critical water-quality projects, the NMFA provides DWSRLF borrowers with low-cost, fixed interest rates.

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 10		[12/31/2020] – Review Date

1. Public systems, including those incorporated under the Sanitary Projects Act, will be offered an interest rate of 1%, which is inclusive of a 0.25% administrative fee paid to NMFA for loan servicing.
2. Public water systems that meet Disadvantaged Entity or Severely Disadvantaged Entity criteria may be offered up to \$1,000,000 at an interest rate of 0%, plus an administrative fee of 0.25% paid to NMFA for loan servicing.
3. Private, non-profit systems will be offered an interest rate of 3%, which is inclusive of a 0.25% administrative fee paid to NMFA for loan servicing.
4. Private, for-profit systems that meet the federal definition of “Public Water Supply System” will be offered an interest rate of 4%, which is inclusive of a 0.25% administrative fee paid to NMFA for loan servicing.

## VIII. UNDERWRITING CRITERIA

A. Debt Service Coverage. The NMFA structures DWSRLF loans to allow for some decline of the Pledged Revenue without affecting the borrower’s ability to pay debt service. Based upon certain factors such as revenue stability and management history, the NMFA may require higher Minimum Coverage Requirements and Additional Bonds Tests, as determined by the NMFA Board of Directors.

1. Historical Revenues. The NMFA will structure its DWSRLF loans so that at a minimum, historical revenues will exceed the Maximum Annual Debt Service (MADS) due during the life of the loan by the following Minimum Coverage Requirements:

a. Gross Receipts Tax	115% of MADS (1.15x)
b. Mil Levy	115% of MADS (1.15x)
c. Net System Revenues	120% of MADS (1.20x)
d. General Obligations	100% of Annual Debt Service (1x)
e. For profit systems	135% of MADS (1.35x)

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 11		[12/31/2020] – Review Date

2. Projected Revenues. The NMFA may consider estimated or projected revenues to determine Minimum Coverage Requirements if a three-year historical average is either not available or if circumstances have changed significantly within the last three years that would justify the forecasting of revenue growth to satisfy the Minimum Coverage Requirements. For example, an entity may have imposed increases in its user rates that are not reflected in financial statements. Under these circumstances, the NMFA will structure its loans so, at a minimum, the borrower’s projected revenues will exceed the MADS due during the life of the loan by the following Minimum Coverage Requirements:

- |                        |                      |
|------------------------|----------------------|
| a. Receipts Tax        | 125% of MADS (1.25x) |
| b. Mil Levy            | 125% of MADS (1.25x) |
| c. Net System Revenues | 130% of MADS (1.30x) |

**B. Additional Bonds Test.** NMFA recognizes that public entities must utilize all legally available revenue streams to fund their governmental services and secure funding for their public projects.

1. The NMFA will allow borrowers to incur additional parity debt resulting in a Parity Lien to a DWSRLF loan, provided the borrower collected, in any 12 consecutive month period during the past 24 months, sufficient revenue to exceed the following Minimum Coverage Requirements, including both existing and proposed debt:

- |                             |                                     |
|-----------------------------|-------------------------------------|
| a. Gross Receipts Tax       | 115% of MADS (1.15x)                |
| b. Mil Levy                 | 115% of MADS (1.15x)                |
| c. Net System Revenues      | 120% of MADS (1.20x)                |
| d. General Obligation Bonds | 100% of Annual Debt Service (1.00x) |

## **IX. LOAN REFINANCING POLICY**

**A.** While certain high cost debt can hinder essential new water system improvement projects, federal guidelines restrict the circumstances under which

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 12		[12/31/2020] – Review Date

the DWSRLF may refinance existing loans. The following are required for a DWSRLF loan to be eligible for refinancing:

1. The refinancing occurs in connection with a “new money” project;
2. The loan proposed for refinancing must have been originated no earlier than 1993;
3. The project financed by the original loan must have undergone a public review process that is consistent with the SERP, including concurrence by all requisite state and federal consulting agencies;
4. The environmental effects of the project must have been analyzed and studied in a manner consistent with the SERP; and
5. The project financed by the original loan must have been used for a purpose consistent with the eligible purposes defined by federal regulation and must have complied with all applicable state and federal regulations.

B. Private entities are not eligible for loan refinancing.

## X. REFERENCES

### A. Statutes, Regulations and Rules:

1. Safe Drinking Water Act – [Title XIV of the Public Health Service Act] [Section 1452 – State Revolving Loan Funds]
2. Drinking Water State Revolving Funds - [CFR Title 40 Chapter I Subchapter B Part 35 Subpart L]
3. EPA’s Interim Final Rule for the DWSRF - [CFR Title 40 Parts 9 and 35, FRL–6846–5, RIN 2040–AD20]
4. Office of Management and Budget’s *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (known as the “Uniform Guidance”) - 2 C.F.R. Part 200 - Requirements for Pass-Through Entities

Dept. – Water Resources	DRINKING WATER STATE REVOLVING LOAN FUND – LOAN MANAGEMENT POLICIES	[6/27/2019] - Effective Date
Project and Loan Policies		4/27/2006 – Original Effective Date
Page 13		[12/31/2020] – Review Date

5. New Mexico Drinking Water State Revolving Loan Fund Act - [6-21A-1 to 6-21A-9 NMSA 1978] Laws 1997, Chapter 144, Section 1

**B. Policies or Program Documents**

1. Memorandum of Understanding – the agreement between the NMFA and the NMED (DWB) to carry out the provisions of the Drinking Water State Revolving Loan Fund Act.
2. Memorandum of Agreement – the agreement between the NMFA and the NMED Construction Programs Bureau to perform engineering and construction oversight.