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INTERAGENCY COMMITTEE ON SCHOOL CONSTRUCTION

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CHAIRPERSON

August 18, 2015

Ms. Sheila McDonald
Executive Secretary
Board of Public Works
Louis L. Goldstein Treasury Building
Room 117
Annapolis, MD 21401

Re: Annual Report on Alternative Financing

Dear Ms. McDonald:

The Interagency Committee on School Construction (IAC) is required to submit by October 1 of each year a report on alternative financing of school construction projects (Education Article, §5-310(C)). Concurrently, under Executive Order 01.01.2014.06, by September 1 of this year the IAC is required to submit recommendations on the funding and financing of public school construction, including alternative financing. As the scope of the second task is broader than the first, we propose to combine the tasks, but we will require an extension in order to complete both. The funding-financing study that has resulted from the Executive Order is in process, as this outline of past, present, and anticipated activities will show.

Following issuance of Executive Order 01.01.2014.06 in May 2014, staff of the IAC met throughout the summer with staff members from the Department of Budget and Management, the State Treasurer's Office, the Department of Legislative Services, the Governor's Office, and the Maryland Energy Administration. This initial exploratory stage involved:

- A roundtable discussion on June 25, 2014 with representatives of local boards of education and local governments to listen to their concerns and receive preliminary feedback on broad concepts.
- Research into the funding and financing practices of other states in the nation.
- Detailed discussion with officers from the Maryland Energy Administration (MEA) on a variety of financing options.

At the end of the summer, it was determined that a value-capture approach oriented around energy savings offers the most productive line of research. We hypothesized that expanding the energy performance contract (EPC) model, already practiced in about one-third of Maryland LEAs, to a regional or statewide scale could lead to substantial project development, design, procurement, and construction savings. Through these savings, a larger number of energy projects could be carried out at lower cost. There are multiple benefits to an expanded energy savings program: reduction of the energy budgets of the school systems will free up valuable operating resources for other purposes while providing a better learning environment for students; reduced energy consumption in Maryland's 1,400-school fleet of buildings will help the state achieve its energy goals and reduce the environmental impacts from consumption of fuels; and an expanded market for energy projects might promote renewable energy sources, including wind and solar.

While achievement of energy savings is an undeniable good, our ambition is broader: recognizing that the backlog of public school capital needs far exceeds the available State and local resources, we have speculated as to whether energy savings can be developed into a revenue stream to support a long-term, self-funded capital projects program. Financing instruments like the revolving loan fund or capital leases might be used in such a program to fund projects at costs affordable to local jurisdictions, while allowing the program to grow in size and scope over time. Such a program, if managed by a third party entity that could access investment funds, would be parallel to and in addition to the conventional assistance provided through the State's Capital Improvement Program and other capital funding programs.

To test these concepts, a small working group of LEA and local government officers met on December 11, 2014 to review potential financing models and discuss local concerns. Following this discussion, the IAC met a number of times with staff of MEA and the Maryland Clean Energy Center (MCEC) to develop the model. The IAC brings to the discussion a knowledge of the capital funding needs of the various LEAs; MEA brings expertise in energy conservation and financing tools; and MCEC staff has broad experience working with public entities and the financial community to establish realistic, workable funding/financing deals in the realm of energy conservation and renewables. The group met on July 7, 2015 with four energy service companies (ESCOs) for preliminary discussions on issues ranging from project types to potential savings, and on July 16 with five LEA representatives to learn more about the local perspective on procurement, standardization of specifications, control over project execution, and willingness to participate in further research.

The discussion among the IAC, MEA, and MCEC has resulted in two concurrent investigations:

1. Modeling of Energy Savings and Costs. In the spring of 2015, MEA submitted a grant application to the U. S. Department of Energy (DOE) to conduct an energy assessment of a sample of approximately 140 public schools in Maryland, and to assess at a detailed level the cost of energy-related improvements for a subset of this sample. The study will help to determine the overall potential energy savings in all Maryland public school buildings as well as the cost of the improvements needed to capture these savings.

MEA anticipates hearing shortly from DOE on the status of the application request. If the grant is approved, we will work closely with MEA to identify the sample schools, conduct the assessments, and analyze the results. This phase will likely last well into the spring or summer of 2016.

2. Real-Project Test of Financing and Implementation. Concurrently, we will request that LEAs provide comprehensive lists of the energy-related projects that have already been identified in their Capital Improvement Programs and other funding programs, as well as in their Comprehensive Maintenance Plans. These projects might range from replacement of single pieces of mechanical equipment to the full upgrade and replacement of an entire HVAC system at a school. Other building systems such as lighting, electrical, and building envelope will likely be included in the list. With this schedule of anticipated but not yet funded projects, MCEC will pursue further discussions with the financial community to gauge the level of interest in investing into a broad energy-savings program. Additional conversations will also be held with the ESCOs to better understand their capacities, the financial benefits of expanding to a regional or statewide program, and how the varying requirements of the individual jurisdictions can be honored while still achieving the benefits of scale and standardization.

These two parallel studies are mutually reinforcing: If the potential savings from the first study are found to be large, and we also find that there is realistic interest on the part of the financial community and the ESCOs, the next step will be to conceptualize the financing instruments and the organizational structure that can leverage the savings into a larger number of energy projects or,

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ideally, into other types of school construction projects as well. Critical questions regarding organization, procurement, program and project management, measurement and verification, and financing instruments will be addressed.

We envision that the two studies will converge in the spring of 2016. In the summer of 2016 a determination will be made as to the viability of the concept we are pursuing. If the concept appears to have validity, we will then develop recommendations for the Governor and the General Assembly in collaboration with our partners at MEA, MCEC, the State Treasurer's Office, the Department of Budget and Management, the Department of Legislative Services, and others, including the Department of General Services Energy Division. If all goes as envisioned, I anticipate that recommendations will be ready in preliminary form by September 1 of 2016.

I hope that this description of the current status of the funding-financing study that emerged from Executive Order 01.01.2014.06 will provide justification for our request for an extension to the requirement to submit a report on alternative financing by October 1, 2015. We will of course keep you informed as this study moves forward.

Best Regards,



David Lever, R.A., D.A.
Executive Director
Maryland Public School Construction Program

cc: State Superintendent, Lillian M. Lowery, Chair, Interagency Committee on School Construction
Secretary David Craig, Member, Interagency Committee on School Construction
Secretary Gail Bassette, Member, Interagency Committee on School Construction
Mr. Timothy F. Maloney, Member, Interagency Committee on School Construction
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