
SELF-FUNDED PERFORMANCE CONTRACTING PROGRAMS



The Energy Services Coalition offers a collection of tools that represent Best Practices for state energy offices (SEOs) to launch and administer programs to increase energy efficiency through energy performance contracting. The documents draw from successful programs in various states and are continually updated to incorporate the latest strategies. They can be easily customized to meet the needs of any SEO or similar government department.

DESCRIPTION: After Start-Up Program Costs, savings can pay for your program costs to offer technical assistance. The states of Washington and Kansas have successfully applied this approach and details of their approaches are provided.

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Just as a performance contract pays for equipment upgrades and related services through the resulting cost savings, it can pay for an oversight fee to cover the state's program costs. A modest fee can be added as just one more cost element in the performance contracting project cost to be financed and paid for through the guaranteed savings stream.

This can be a winning strategy for the oversight agency, the client and even for the ESCO. Cash-strapped state energy offices (or general services administration departments) can use the funds to provide needed technical assistance to clients. Clients pay for the service through savings so incur no out-of-pocket expense and, with the built-in technical support from the oversight agency, have a much easier time initiating and implementing a performance contracting project. From the ESCO's perspective, there is a down-side that some savings have to cover this added cost but the upside is that more clients come on-board and knowledgeable clients with a streamlined procurement and contracting approach cuts marketing and legal costs.

Two states – Washington and Kansas – are successfully using this approach.

Successful State Examples

State of Washington

The State of Washington, through its Department of General Services and Administration (GSA), pioneered the self-funded program approach in 1983 by charging a fee to clients in return for program

services. The program is now 100% self-funded at about \$2 million annually which covers the costs of 11 state employees and other program expenses.

Washington's very in-depth services include: 1) program administration to pre-qualify ESCOs and establish state-approved contracts, ESCO selection assistance, engineering oversight of the audit, performance contract documents, and monitoring and verification process; 2) contract negotiation of technical, financial and legal issues; 3) construction management oversight through the design, construction and commissioning process; 4) shared risk, as the state actually holds the agreement with the ESCO on behalf of the client. A sliding fee schedule ranges from 1.4% for a \$4-5 million project to 6.6% for a \$200,000 - \$300,000 project. For smaller or larger projects, the fee is negotiable. (See attached Fee Schedule.) Fees are collected at the end of the construction period. Clients include state departments school districts, cities, counties and other state and local government entities.

State of Kansas

The State of Kansas, through the Kansas Corporation Commission's Facility Conservation Improvement Program (FCIP), established a fee-based approach in the initial roll-out of its performance contracting program. Fees range from 4% for a \$100,000 project, to 3.3% for a \$300,000 project, to 1.3% for a \$5 million project, to .74% for a \$17 million project. (See attached Fee Schedule.) After several years of operating the program substantial funds started rolling in and the FCIP was in the favorable position to decide how to make use of those funds - apply funds as a potential buy-down to help the cash-flow of renewables in performance contracting projects, bring on technical assistance contractors, or expand the program in other ways.

Important Criteria to Establish a Self-Funded Fee-Based Program

- Contact ESC for technical support from web-based tools and our State Technical Support Liaisons.
- Ensure performance contracting is an option for state government. Most states have enabling legislation or administrative rules that authorize performance contracting as a funding mechanism, or have a pilot project in place that already tested the legal issues. Establish consensus among procurement, legal, finance and buildings departments to work through any other barriers for state departments (and local governments) to do performance contracts. Also investigate if local governments have this capability.
- Investigate authority to assess and receive funds from other state departments as well as non-state entities. In the absence of direct legal authority, here are some tips: 1) Apply the approach used by other state departments where the groundwork for inter-agency payments has already been laid. Typically another state department, such as the legal or IT department, receives payment for services provided to other departments. 2) Apply a reimbursement strategy. Provide technical assistance through paid contractors, then invoice for reimbursement. There may be no need to gain authority for a reimbursement payment. The differences with this approach are the delay of payments, that only contract services may be eligible and efforts of staff may not qualify for reimbursement payments, and that maximum payments are linked to justifiable reimbursement payments. 3) Further explore the ability to work with non-state entities in this way as there may be fewer obstacles.

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- Determine the level of services to be provided. Minimal services include: pre-qualified list of ESCOs and process to select the finalist, with pre-approved maximum markups for each ESCO; pre-approved contract templates; project development guidance; engineering assistance to review and make recommendations on the audit and contract documents ; and monitoring and verification oversight. ESC's tools and resources can help launch these efforts. Additional services could include: technical oversight of design and construction process and documents, formal acceptance of documents, a greater degree of technical assistance, etc.
 - Determine the fees to be assessed. Refer to the Washington and Kansas examples attached. Fees are inversely proportional to the size of the project – smaller projects can take just as much up-front project development time as much larger ones. Consider the impact on very small projects and have a negotiable rate.
 - Establish roll-over authority so that funds that are received but not used in a fiscal year can be rolled over for use in subsequent years.
 - Determine when to begin assessing fees. Initiate fees at the onset of the program, identify a future time when fees will be assessed (this has the added benefit of incenting clients to get started early and avoid the fee), or have a phased approach based on market sector where smaller projects may be excluded.
 - Recognize that it will take over 3 years to approach a fully self-funded program. The first year may involve program start-up activities to pre-qualify ESCOs, get contracts pre-approved and work through other legal and finance issues. An educational campaign may be needed to bring-in potential clients during the first year after the program is launched. Once clients sign-on, the fees cannot be collected until construction is completed which may be 15 months from the first contact with a client. This timeline includes the time a client needs to decide to do a performance contracting project, select an ESCO, enter into an audit contract, review the audit, negotiate and finalize the performance contract, participate in the design process, and oversee construction to its end. Fees are usually collected at the end of construction and are made available as part of the overall financed project.
 - Plan how to start-up and sustain a program during the first several years before collecting fees. Identify a program manager or point person to develop the program. ESC's resources and technical assistance, in conjunction with mentoring from other states as facilitated by ESC, can offset much of the start-up cost and reduce the program development time.

SAMPLE FEE SCHEDULES

State of Washington (early 2009)

Total Project Value	Project Management Fee	Percentage of Cost	Termination
\$5,000,000 or More	Negotiate		Negotiate
Below:			
\$5,000,000	\$68,800	1.4%	\$25,500
\$4,000,000	\$64,900	1.6%	\$23,600
\$3,000,000	\$59,900	2.0%	\$21,700
\$2,000,000	\$52,800	2.6%	\$19,600
\$1,500,000	\$47,800	3.2%	\$17,150
\$1,000,000	\$40,800	4.1%	\$16,150
\$900,000	\$38,900	4.3%	\$15,000
\$800,000	\$36,900	4.6%	\$13,950
\$700,000	\$34,600	4.9%	\$12,800
\$600,000	\$31,900	5.3%	\$11,500
\$500,000	\$28,700	5.7%	\$10,100
\$400,000	\$24,800	6.2%	\$8,800
\$300,000	\$19,800	6.6%	\$7,300
\$200,000	Hourly Cost		Hourly Cost

State of Kansas (early 2009)

FCIP FEE SCHEDULE	1st \$100k	Next \$400k	Next \$500k	Next \$4m	Over \$5 m	Fee Total	Fee %
	4%	3%	2%	1%	0.5%		
Total Amount of Project	\$0-100k	\$100k-\$500k	\$500k - \$1m	\$1M - \$5 M	Over \$5 M		
\$ 100,000	\$4,000	\$0				\$4,000	4.00%
\$ 200,000	\$4,000	\$3,000				\$7,000	3.50%
\$ 300,000	\$4,000	\$6,000				\$10,000	3.33%
\$ 400,000	\$4,000	\$9,000				\$13,000	3.25%
\$ 500,000	\$4,000	\$12,000	\$0			\$16,000	3.20%
\$ 600,000	\$4,000	\$12,000	\$2,000			\$18,000	3.00%
\$ 700,000	\$4,000	\$12,000	\$4,000			\$20,000	2.86%
\$ 800,000	\$4,000	\$12,000	\$6,000			\$22,000	2.75%
\$ 900,000	\$4,000	\$12,000	\$8,000			\$24,000	2.67%
\$ 1,000,000	\$4,000	\$12,000	\$10,000	\$0		\$26,000	2.60%
\$ 2,000,000	\$4,000	\$12,000	\$10,000	\$10,000		\$36,000	1.80%
\$ 3,000,000	\$4,000	\$12,000	\$10,000	\$20,000		\$46,000	1.53%
\$ 4,000,000	\$4,000	\$12,000	\$10,000	\$30,000		\$56,000	1.40%
\$ 5,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$0	\$66,000	1.32%
\$ 6,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$5,000	\$71,000	1.18%
\$ 7,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$10,000	\$76,000	1.09%
\$ 8,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$15,000	\$81,000	1.01%
\$ 9,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$20,000	\$86,000	0.96%
\$ 10,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$25,000	\$91,000	0.91%
\$ 11,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$30,000	\$96,000	0.87%
\$ 12,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$35,000	\$101,000	0.84%
\$ 13,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$40,000	\$106,000	0.82%
\$ 14,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$45,000	\$111,000	0.79%
\$ 15,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$50,000	\$116,000	0.77%
\$ 16,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$55,000	\$121,000	0.76%
\$ 17,000,000	\$4,000	\$12,000	\$10,000	\$40,000	\$60,000	\$126,000	0.74%