

# **ECONOMIC OPPORTUNITY STUDIES**

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## **Should Weatherization Assistance Program Delivery Agencies Leverage their Skills by Offering Services to the Private Market?**

In any given year, there are dozens of local Weatherizers undertaking services for the “market” of conventional, i.e. non-eligible residences and in some areas for small commercial buildings. This fee-for-service has been tested for about twenty years, always with DOE’s active support and encouragement. There are far fewer weatherization providers that have active affiliated businesses, even not-for-profit corporations, set up primarily to market energy services.

Our EOS Leveraging Partnership has informally collected information on these initiatives through training events, written reports, and interviews. At present, at least some of the agencies in NY, OH, PA, WA, OR, and NV do have active legal entities separate from the parent 501(c)3 pursuing this kind of private sector energy work; at least one other state WAP network is gearing up for a “private market initiative.”

### **Issues to Consider**

#### **➤ Agency Mission**

It is important to understand local Weatherization providers are different from private ESCOs and individual entrepreneurs. The WAP local agencies are all private nonprofit or local government organizations.

The 501(c)3’s must by law ensure that nearly all their resources are devoted to their charter purpose. The governmental agencies are even more constrained. They cannot undertake ventures that risk undermining their ability and resources to produce all the results they are set up to deliver for the communities they serve, however these may be defined.

This actually aligns them with the general purposes of the federal government in that:

- They should never participate in activities which do not serve the public interest, in this case not in ineffective energy investments no matter what the market wants.
- Not should they undertake activities that detract from their ability to serve low/moderate income communities.

- Therefore they consider the following when deciding about establishing “market” oriented or “fee-for-services” subsidiaries.

➤ **Understanding the Nature, Scope and Goals of Local WAP Agencies**

Nearly every Weatherization agency is a multipurpose agency, not an energy-only organization. A number are “only” housing and community development organizations. However, more than 700 are CAAs, multipurpose agencies that also provide a variety of social services and related community investments; based on NASCSP’s annual CSBG report we can estimate they managed 2005 programs that collectively totaled \$5.5 billion. Obviously WAP, even with leveraging, is only part of a bigger community agenda.

CAAs leverage very successfully. More than 35% of their total funding comes from non-federal sources. More than a third of those funds represent private financing for services or in-kind donations. These resources are obtained by sustained engagement by the agencies’ leaders in advocating for and implementing partnerships with utilities, governments, and developers (examples at [www.weatherizationplus.org](http://www.weatherizationplus.org)). This track record may contribute to securing far more funding for their WAP-type activities by going straight for partnered investment resources to “piggyback” with weatherization services, i.e. to delivery in an integrated package. So far, Weatherizers in states seem to have leveraged more than \$200 million in “private” funding of which most comes from mandated utility contracts financed by rate-payers.

➤ **Institutional Risk Considerations**

Establishing what might loosely be termed a “for-profit” arm, the one that brings in revenue from private market sales that can be devoted to the agencies’ core purposes requires that substantial (nonprofit) legal and organizational resources be invested. (These requirements and procedures are thoroughly covered by the trainers that DOE and other organizations sponsor. Their material is available.) Making such an investment of an agency’s scarce development resources requires that its leaders be assured that the result will be self-supporting and enhance its other charitable/public purpose activities.

## **New Affiliate v. Program Services**

➤ **Federal Legal Barriers (and related costs)**

All activities must be paid for without any federal subsidy for two reasons:

1. (Obviously) WAP funding is only for eligible homes, but also
2. Federal funds may not be used to lower the costs of work that is competed against non-subsidized private businesses.

As a result, numerous states (or cautious local counsels) prohibit any use of WAP equipment, trucks, or storage space and other indirect costs. They could allow these costs to be prorated between WAP and "market" uses by following OMB requirements set out in cost allocation rules. Most leveraged programs cost-allocate, but the fiscal monitoring cost and the potential for error has led some program managers to avoid the risks. In those locations, a local agency would have to maintain a separate set of WAP-like infrastructure elements for its "market-oriented" enterprise – an unattractive option, especially absent some certainty of a multi-year market demand. The market instability is discussed further below.

➤ **Competing with Agency Contractors for Market-Rate Business**

We estimate roughly half the WAP workforce comes from the private local contractors WAP trains and employs, (EOS, 2002). Weatherization agencies consider their training contribution to this private workforce as a major investment in deploying more advanced energy efficiency skills and tools. For the contractor-based programs, the choices are to assemble a contractor-based team and bid for "market" business that the contractors might win alone or to compete against one or more of their own trained contractors.

Many would consider such moves contrary both to their mission of deploying high-level skills to the local private home contracting market (at contractors' expense), because of the promise made that skill will "pay off" for the entrepreneurs, as well as contrary to their more general mission of developing the local economy.

➤ **Conflict with Community Action or Local Government Development Priorities**

Given the costs and risks of setting up a new "market" entity, all the organizations weigh the alternative uses of their leadership's time, the legal costs, and their public support and then compare other options for achieving their mission with new ventures.

➤ **Profit Potential**

The program income expectations should be low.

## **Lessons Learned by the Agencies with Not-for-Profit Subsidiaries**

➤ **The Markets for WAP Services are Unstable**

○ The General Homeowner Market

Weatherizers offer a more sophisticated diagnostic system and a more comprehensive set of investments than the building rehab industry standard or than most utility programs. The "general public" is likely to consider the improvements as a home

improvement and seek bids from known local contractors including, perhaps, the WAP agency. A more educated public more willing to spend what is needed is the missing ingredient in the resident market.

This holds true for nonprofit low-income housing developers as well, as discussed; that group is a prime target for DOE to persuade or for HUD to direct.

- Multi-family building owners are more likely to go to ESCOs whose services are more comparable in cost and depth to the WAP agency but who are also more likely to include work by licensed trades for commercial-sized HVAC and wiring in the package. Many of WAP's licensed contractors are primarily skilled in residential small-scale building. Further, ESCOs may finance based on shared savings, requiring a depth of capital not generally available to smaller not-for-profit ventures.

Both sets of competitors, home remodeling contractors and ESCOs, create downward price pressure on the WAP venture. The parent agency has only one reason (other than doing a good job) to be interested in such an initiative: creating a revenue stream to support its public purposes. A financially risky venture is of little use and may actually threaten achieving its purposes.

➤ **Niche "Private" Markets are Far More Promising but Elusive**

Policy initiatives at the state or utility service territory level have created potential niche markets beyond the eligible population. WAP providers have actively pursued and are, today, actively pursuing several. Notable examples both failed and successful:

- The OH HERS experiment: In the mid-90s, OH Weatherizers, as well as private contractors, had many of their staff trained to use the state Home Energy Ratings System (HERS) designed to support energy-efficient home mortgage lending. While a handful of such mortgages were made, the lending community did not buy into it nor market the concept to homebuyers, and the initiative petered out. Many (frustrated) raters still work in our network.
- Utility DSM or System Benefit Funded Investment for Higher-Income Households  
A far more stable market is a utility system's required investment in some kind of Weatherization activity in homes that are not low-income. In those programs where audits or installation of certain measures or appliances are paid for by the utility, risks to

agencies' success are far lower. A public bid process is typical for such programs; utilities as well as NCAF's Leveraging Conferences have offered training in the bid procedures, as these differ from the public sector or charitable funder competitions in which these agencies have such deep experience.

These opportunities are far from wide-spread. Many states have established residential DSM initiatives that do not deliver direct services, but rather provide equipment or materials rebates or install "smart" energy controls using the utility's licensed workforce. Too many other utilities directly deliver services that Weatherizers believe to be either ineffective or of short duration. An example is superficial "audits" that involve checklists and air infiltration inspection, but lack a serious methodology for estimating the savings from alternative packages of work. They are equally suspicious of projects that drop off low-cost, no-cost kits and provide generic energy "public information." Every year, a significant number do undertake such activities for various reasons (the "request of the Governor" is perhaps the common explanation) but attracting these revenues might actually undermine their reputation for getting results and for their broader mission, changing the housing/community infrastructure.

At present, one state with a serious program of installations in "market" housing is OH. Many OH Weatherizers have set up separate entities to participate as subcontractors to teams of private entities competing to be prime contractors in the 2007 DSM round.

➤ **One Market is a Natural for WAP Housing Developers**

○ Housing/Community Development Opportunities

(No WAP funds can be used for new construction, of course.)

The CAAs and others who are directly developing new or rehabilitated low-income housing (not a majority of agencies) do have separate not-for-profit "arms" for the purposes of financing and packaging development capital, marketing tax credits, and so forth. It is common for these corporations to contract with their parent agency's WAP workforce to seal, insulate, and later audit buildings under construction. Projects currently wrapping up in Reno, NV come to mind. The developers are paying the WAP agency for the energy investments in homes under construction. NHS in Toledo often has such projects underway.

○ Partnering with Other Housing Developers

Partnerships with other organizations that are not-for-profit developers are multiplying. The "Habitat" development in central MA that contracted with the WAP agency is one of several.

## **Summary**

The opportunity to take part in the private home improvement market jobs that deliver residential efficiency has been interesting to local Weatherizers and to most federal managers for more than twenty years. Over time, the network has honed its capacity to distinguish the opportunities which truly will result in a gain for the community at large and for the WAP program. There is continuing demand for sharing best practices and legal/management support so that the occasional "good opportunity" in a new market can be seized.

The development of more financing packages that anticipate building sound energy features into homes would create a market for quality work. A caution: there are far fewer federally-subsidized units built or rebuilt than there are WAP units each year, and some states may have none.

## **The Department's Role in Encouraging Private-Market Opportunity**

DOE-WAP has supported top-notch training (at the DOE-supported NCAF Leveraging Conference and at many DOE regional and national Conferences) in the organizational and management expertise involved in setting up fee-for-service areas. Two of the most highly acclaimed trainers are Susan White of AZ and Greg Thomas of NY.

The office also supports a leveraging information-gathering/exchange/training process through our project, NCAF conferences, and other sub-national efforts. This work generally leads to projects in which WAP agencies become the workforce for more of the low/moderate income utility delivery programs, a market with significant growth potential even now, and partners with housing developers. A major priority for Weatherizers is to find resources to leave Weatherized homes in excellent overall condition.

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