

Applying the Notion of Community in the Commercial Sector

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ABSTRACT

Understanding and harnessing the power of community—both geographic and psychographic—is a fairly new focus for residential energy-efficiency programs. While targeting specific communities may be a part of strategic marketing campaigns, it is not common in residential or commercial energy-efficiency programs. This paper explores how defining and understanding community may be equally requisite for commercial energy-efficiency programs, especially for those programs intended to reach traditionally underserved markets.

Small and medium-sized businesses in the food industry—independent restaurants, convenience stores, and grocers—is a market with large energy-efficiency potential that has not participated in traditional efficiency programs.

The Cadmus Group (authors) recently examined this market to inform the design of a commercial energy-efficiency loan program. We conducted interviews with market actors and trade allies, such as utilities and contractors, whose success with these businesses has varied greatly. We also interviewed representatives of the many trade associations (restaurant, grocers, food and beverage, licensed beverage, and convenience stores) these businesses rely upon. Through these trade associations, we conducted surveys of their community members to further understand them and how to serve them better.

In our research, we have discovered a rich community with both barriers and opportunities. These businesses often distrust government; have no time for paperwork; and apply business practices from diverse cultural backgrounds. They rely on face-to-face relationships, word-of-mouth, and fax machines more often than the Internet, and they prefer “let me see and touch it” approaches. They are interested in saving money but have paid little attention to energy efficiency. Independent food businesses may not be aware of the fact that energy bills are one of their controllable costs. Other utility-sponsored programs serving this sector have shown that savings can range from 3% to 18%. A program in the Northwest focused on refrigeration savings in grocery stores and achieved approximately 39 million kWh. The potential to achieve energy savings in this sector is large and certainly worth pursuing. These savings in energy expenditures will free up money for other purposes, such as keeping a business operating, expanding a business, or revitalizing the community.

This paper will discuss ways to understand food business communities and the program strategies that are needed to serve them successfully.

Introduction

Energy-efficiency financing programs designed for the commercial sector are growing in popularity, and especially those targeted to small businesses, since they are often strapped for capital. These financing programs use a variety of mechanisms to identify potential loan signatories, and they come with many different features in loan products (Bell 2011; Hayes 2011). They are intended to mitigate the perpetual up-front cost barrier for energy-efficiency improvements; some programs are marketed or designed so that the savings in energy pays the

financing fee. However, experience has shown these programs face implementation challenges, especially in understanding the communities of businesses within particular market segments. These programs need to improve coordination with various market actors, including the lenders, loan program administrators, trade associations, the utilities serving customers, and contractors (e.g., auditors, equipment vendors, and installers).

This paper summarizes findings from market research that Cadmus conducted for a Michigan nonprofit organization that was designing and implementing a commercial loan program to finance energy-efficiency improvements. The loan program targets small independent groceries, restaurants, convenience stores, and other establishments that sell food (independent food vendors). These businesses operate on a slim margin and have been particularly hard hit by the economic downturn. The overall purpose of our market research was to present a broader picture of the independent food market and to identify barriers and opportunities for financing energy-efficiency improvements in this sector.

We reviewed secondary research about this sector, analyzed the geographic distribution of retail food sector businesses, and interviewed or surveyed 118 key market actors such as representatives from trade and contractor associations, utilities, contractors that could supply energy-efficiency services, and independent food vendors. (Independent food vendors responded to an on-line survey. Interviews with all others were conducted either in person or by phone.) Overall, our data indicate that Michigan's retail food industry is a community that:

- Has considerable potential to improve the energy-efficiency of facilities and equipment
- Has interest in making efficiency upgrades
- Needs financial assistance tailored to their needs
- Is built on important existing relationships that need to be understood, involved, and leveraged to increase trust among program actors and the groups they are targeting

Building relationships and increasing trust within the independent food industry is essential to bringing the benefits of improved energy-efficiency. This community is built on relationships, which may be familial, ethnic, or unique because of the common experience of running the business. Word-of-mouth, peer-to-peer education, and testimonials are important means of communication. These businesses tend to trust each other rather than feel they are in competition. We also found:

- Trade association managers and members agreed that the independent food businesses turn to their associations for guidance on issues that affect them.
- Few businesses think about the potential for saving money through energy-efficiency. Energy-efficiency is not a priority but keeping the business afloat is.
- Many businesses do not understand what energy-efficiency options are available.
- Businesses do not have the time or capital to invest in energy-efficiency upgrades.
- Businesses might be convinced that saving energy is a good deal if their peers participate in the rebate or loan program, if it is simple, and the payback is short.
- In addition to a loan, businesses would like to leverage utility rebates, tax credits, or economic development grants or funding sources to help make the energy-efficiency project affordable.

- If businesses and trade associations think about energy, they think about gas before electricity because they usually hear about gas more often. Because Michigan is a customer choice state, vendors regularly approach businesses to try to convince them to switch gas suppliers.

Energy-efficiency Upgrades Are Likely

In 2010, Cadmus conducted a baseline study for the state of Michigan to identify the equipment installed in food industry establishments and to examine the likelihood the business would upgrade to energy-efficient equipment (Cadmus 2011). In the baseline study, we asked businesses if they expected to make such an upgrade sometime in the next two years. A subsequent online survey asked businesses if the upgrade would occur in 2012 (within one year).

Overall, the baseline study showed 52% of grocery stores and 65% of restaurants were likely to make such an upgrade within two years. The online survey found about 49% of all respondents stated they were very likely to make an energy-saving upgrade within the next year. Of the online survey respondents, 48% of grocery association members and 52% of all other respondents were likely to make upgrades in the next year. Overall, the online survey found about 72% of respondents were either *somewhat* or *very likely* to make an energy-saving upgrade. These results confirm at least half of food-related businesses are interested in making energy-efficient improvements in the near future and this interest creates opportunities for a loan program.

Our study established that there are approximately 7,500 independent food businesses in Michigan with fewer than 50 employees and less than \$5 million in annual revenue. Restaurants are the largest share by far, followed by grocery stores, convenience stores, and wholesale food vendors. Most are located in and around Detroit and in cities in the southern portion of the state. The opportunities for energy savings are strong because these businesses are often energy intensive and, as noted, half of the survey respondents stated they are considering upgrades. The nonprofit loan program has an initial goal of 250 loans, which is about 3% of this traditionally underserved market.

Trusted Messengers and Relationships

Providing a financing program for Michigan's independent food vendors will require a web of interrelated services from various market actors. This section discusses what we found about who food businesses trust and the nature of the existing relationships with those they trust and distrust.

Trade Associations

When the Michigan nonprofit is ready to launch the commercial loan program statewide, they will need to spread the word to the target market segment, recruit customers, and ensure that auditors and contractors assist in selling the program. In Detroit alone, one can find many cultural groups; many businesses are family-based and business decisions are not always made by the business independently, but in consultation with family or colleagues. The question then is what is the best way to reach the various businesses.

In interviews with trade associations, we asked specific questions about who food industry businesses trust to provide information about energy-efficiency opportunities, financing for energy-efficiency projects and information delivery in general. The consensus was that businesses trust and rely on their trade associations for information. These associations advocate for their members and provide information and assistance to help their business succeed. Unlike vendors and contractors, the associations are not selling a product.

Some trade association representatives reported their members have a general distrust for utilities and contractors. Some members view information coming from a contractor as “just a sales pitch” rather than sincere advice about improving energy-efficiency and saving money. Unless a business owner knows the contractor, or a colleague has made a recommendation, it is unlikely businesses will let an unknown contractor into their establishment with a pitch for energy-efficiency and a handful of rebates.

The food industry is highly regulated and businesses and associations reported frustration with the government, in general. For example, one respondent explained that the amount of complicated paperwork required to apply for tax credits for alternative energy fuels such as biodiesel was a very large barrier and limited acceptance by their members. (This particular trade association represented gas stations and small convenience stores, hence, the reference to its experience with biodiesel tax credits.)

Contractors

Independent contractors attended one of two training sessions to learn about the loan program so they could conduct program-required energy audits, install approved equipment, and offer the loan program’s financing option to their customers in the city where the pilot had launched. The trained contractors we interviewed reported they typically build their customer bases through networking or referrals. All pointed to the importance of maintaining and building relationships with their customers.

Contractors suggested ways to ensure that the commercial loans help food industry customers install energy-efficiency upgrades. They emphasized that customer awareness is paramount to contractors’ success. Contractors also noted customers could be wary of such loan programs because of financial constraints (i.e., taking out a loan when already in debt or operating with a small profit margin) and because of a lack of trusted relationships in the industry (i.e., customers rely on their utilities or trade organizations for information, rather than following the advice of independent contractors or a program with which they are unfamiliar). To assuage these concerns for both contractors and customers, it is important to provide customers with guarantees about the loan terms, length of financing, and realized savings and to address how contractors connect with potential customers.

Lenders

An important actor for a financing program is the lender. Trade association representatives told us their members typically deal with smaller and more local financial institutions where they build personal associations and trust and get more individual attention. The representatives thought this preference would hold true for other sources of financing such as the loan program. This was echoed by utility representatives and others with experience in the lending community.

Trade Association Members

The online survey offered trade association members an opportunity to tell the nonprofit what is important to them in the design of a commercial energy-efficiency loan program. Respondents rated eight items related to financing as either *essential*, *preferred*, or *not essential*. Of the trade association members who responded to the online survey, we found that two financial factors stood out as having the largest share of “essential” ratings:

- Savings on the energy bill would pay back the investment in three years or less (54%).
- Energy savings would be at least as much as the monthly finance charge (43%).

One factor received the same number of “essential” and “preferred” responses: they could get tax deductions, utility rebates, or other grants to help reduce the costs of the improvements. These three items all directly related to getting the invested money back, ideally in a short time, emphasize the sentiment in the retail food sector that money is tight and financing an energy-efficiency project is only possible if one can quickly and easily offset amounts spent with savings from the upgrade and other credits or rebates.

But Not Everyone Knows About Utility Rebate Programs

Even though utilities launch major marketing campaigns and offer rebates and incentives to nonresidential customers and some programs have been in place for many years, not everyone knows about these programs to encourage consumers to install more energy-efficient products. Many trade association managers we interviewed were unfamiliar with utility rebate programs. They are advocates for their members first and their focus is usually on legislative issues that directly impact their customers.

To its credit and foresight, our nonprofit client contacted trade associations early in the loan program design process. The trade associations, though initially knowing little about energy-efficiency and utility rebate programs, were very willing to reach out to their memberships. They reminded their members of utility rebate programs, launched a survey seeking input that would help tailor the loan program to members’ needs, and provided information about the upcoming loan program. The associations provided insight into their membership to the loan design team that helped to develop an attractive product. The trade associations, because they are a trusted source of information, proved to be an essential conduit for reaching the market segment the loan program wanted to target.

Prior Program Successes Prevailed by Using Community Relationships

In our secondary research, we found examples of successful programs serving the small independent food industry and articles that described the need to build partnerships and provide individual attention and peer-to-peer assistance. This research is described in the next sections.

DTE Energy Independent Grocers Program

DTE Energy, which serves the Detroit area, customized an incentive program for independent grocers, offering a turnkey package that involved outreach, vendor networks,

customer specific measures, and financing. Before launching its customized energy-efficiency program, DTE investigated the nature of relationships in the market. It soon recognized that the grocery market was tightly associated and built on strong family relationships. Business owners were skeptical of the energy savings claims, were not familiar with the technologies, required quick payback on investments, and tended to make decisions as a group.

To educate this customer segment, DTE brought information directly to its customers through one-to-one meetings, case studies, and group presentations. At group meetings, energy-efficient technologies were displayed and demonstrated so business owners could touch and experience firsthand. DTE reports the program successfully overcame hurdles through a collaborative effort among the trade allies, management, and business associations. The program's marketing and outreach was highly customized to include trade associations and community groups.

Through their "deep dive" (as DTE called it) into the grocery segment, DTE reported 50% of its target market attended the kick-off presentation or participated in the program, which was fully subscribed in two weeks.

BPA's EnergySmart Grocer Program

In a 2010 publication, Portland Energy Conservation, Inc. (PECI), and the Bonneville Power Administration (BPA) reported on their work to bring the EnergySmart Grocer program to utilities and grocery stores in the Pacific Northwest (Kramer 2010). This FY2009 program reduced energy consumption for refrigeration in grocery stores. An important note is, even though PECI had seven years' experience administering the program elsewhere, customers in this region required a different approach. The sheer size of the region, the number of utilities, the variety of businesses, and the economic recession all presented challenges. And, while the target market was grocers, PECI stressed that national chains required a different approach than independent stores.

PECI realized that the opportunity for energy savings in this market is large, but its goals could be realized only through close cooperation among program managers, analysts, marketing professionals, contractors, trade associations, and end-use customers. The program required unique and flexible delivery approaches tailored to rural and urban customers. PECI also recognized cultural differences throughout the region (particularly between urban and rural customers) and between chains and independent stores.

The program created partnerships with Northwest grocers' associations, through which the program developed relationships to build trust, spread knowledge, share a common language, and be sensitive to different cultures. The program's customer focus and flexibility contributed to significant energy savings (approximately 39 million kWh). It is important to note that the relationships were not built overnight; the authors reported it took over 18 months for the EnergySmart Grocer program to gain traction.

Local Governments and Local Relationships

A 2012 ACEEE paper discussed opportunities to increase the penetration of energy-efficiency measures by leveraging the attributes of a well-designed partnership (Mackres 2012). This paper discussed the increasing role of local governments, community, and nonprofits in

delivering energy-efficiency services and described the characteristics that contribute to implementation, such as regulatory mechanisms, financial incentives, and local relationships.

Local relationships are considered the trusted messenger of energy-efficiency. We believe this notion of a trusted messenger supports our findings in the Michigan research. Such partnerships lead to better outreach, education, knowledge, and participation. Though the examples in the ACEEE paper were of residential programs, common themes of successful program partnerships apply to nonresidential programs. These are personal guidance, technical support, and relationship management (typically one-to-one); simplified processes; and strong community engagement.

A Number of Options and Observations about Financing Energy-efficiency

The number of financing vehicles for energy-efficiency improvements has grown over the last few years, especially with the American Recovery and Reinvestment Act (ARRA) and the Regional Greenhouse Gas Initiative (RGGI), and other initiatives. There are now many financial vehicles and programs for both residential and commercial energy-efficiency projects (Freehling 2011). As noted in the Freehling paper and echoed in our interviews with market actors and trade allies (contractors, utilities, and trade associations) for the market research in Michigan, commercial banks typically are less interested in financing energy-efficiency projects of small commercial establishments when the loan size is small, often considered risky, and the cost of underwriting and servicing outweighs the return.

In the last few years, there has been an increased focus on commercial loans and outreach to the commercial sectors from such financing vehicles as small community banks, credit unions, nonprofit loan funds, community development funds, state and local governments, and now even large institutional commercial banks. In addition, some utilities offer on-bill financing (Peters 2007; Freehling 2011; Cadmus has evaluated several programs but reports are not yet public).

As we discovered in our Michigan research, community banks and credit unions will likely finance the loans. Not only do they offer smaller loans, their customers appear to be more inclined to work with them than with commercial banks. Interview respondents stated that some commercial banks are calling in loans of customers who are current in their payments, which adds to customers' economic difficulties. The interview responses supported efforts to engage community banks and credit unions to offer financing for a commercial energy loan program.

A white paper published by ACEEE in September 2011 (Hayes 2011) offered observations and findings that support the results from our Michigan research. The white paper discussed the lack of uniformity, standards, and information, which made it difficult for private lenders to evaluate the risk, and finance, energy-efficiency projects. General observations presented in the white paper about financing programs are instructive:

- Most programs are not penetrating the targeted audience.
- Bottlenecks can occur with burdensome program requirements (including contractor qualification, complicated paperwork, slow loan processing).
- Good loan terms do not assure success of the program; packaging programs for ease of participation and marketing the program is important.
- There are no uniform criteria to evaluate credit of small businesses and institutions.

The white paper offered several recommendations to attract broad participation: design the program for a target audience; budget for and invest in ongoing marketing of the program; simplify the loan application process; offer attractive loan terms; package loan programs with utility incentives and rebates; tier program benefits (such as loan terms) to incentivize greater energy savings; train participating contractors to ensure the credibility of the program and the achievement of energy savings.

All of these observations are important to ensure the financing vehicle has optimized its chance of uptake and success. Of particular interest to this paper are the points about *programs not penetrating the targeted audience* and that the programs need to be *designed for the target audience*. While there are many reasons these are true, including those given above, it may also be that there is a geographic and/or psychographic community that is not fully understood. That is, lenders need an understanding of the key attributes of the community, such as its values and attitudes toward financing and energy-efficiency upgrades, and working with financiers, utilities, and nonprofits. Success may require a customized approach to building relationships with the target community. In addition, an investment in marketing over the life of the program is important, as “good loan terms” alone will not guarantee participation. Our research also showed that targeted social marketing, such as neighborhood meetings and local events, are important to recruit participants. Building and maintaining trusted relationships with the targeted community takes time and effort.

So, How Do We Help Design Michigan’s Loan Program?

Market actors report that money is tight in Michigan’s slowly recovering economy and the businesses in the independent food industry are looking for ways to cut costs. They may not be fully aware that energy bills are one of their controllable costs and prior programs have shown that savings can range from 3% to 18%, which frees up money for other purposes.

Both our Michigan baseline study and our market research assessed the financial aspects of making energy-saving upgrades. The questions from survey to survey were not the same, which limits direct comparison; however, we highlight that, among all those surveyed in the baseline study, 59% strongly agreed with this statement: “*Price is the biggest reason why my company might not buy a high-efficiency item.*”

In addition, 67% of grocery owners and 79% of restaurant owners noted that investment decisions about purchasing new equipment were strongly affected by the economic downturn. This echoes the sentiment expressed by food sector businesses in the online survey, where respondents identified the most important aspects of the loans would be in having savings outweigh the monthly finance charge, having a short return on investments, receiving associated tax deductions and utility rebates, and qualifying for loans with a low interest rate that guarantees financing. Both studies reflect the idea that, when making energy-efficient upgrades, money is the most significant potential barrier.

Similarities and Differences in the Preferred Loan Package

When defining elements of a loan program, we found similar themes that will likely make financing more appealing to businesses in the food industry. They are:

- Financing that is easier to obtain than bank loans
- Processes that are easy and simple
- Unsecured loan options
- Competitive interest rates
- Longer loan terms
- Fast payback and return on investment
- Upfront costs that are minimized
- Positive cash flow

Online interviews with trade association members (the ultimate loan recipient) found a similar story, but with different details. These details will be important to customize the approach and messaging when reaching out to the different sub-communities. For example, the following three graphs show the differences for specific questions between two groups of respondents. Our research is ongoing, this sample is small, and results may change with additional respondents. However, the early trend shows key differences between two retail food industry communities.

In Figure 1, more grocery stores (n=50) are likely to finance as the project amount increases, with half likely to finance projects costing \$75,000 or more. The restaurants and gas station mini-stores (n=27) are likely to finance much smaller projects, starting around \$10,000. These respondents reported little difference in their likelihood to finance projects ranging from \$10,000 to over \$75,000 or more.

Figure 1. Likelihood of Financing Energy-Efficiency Projects at Specified Levels

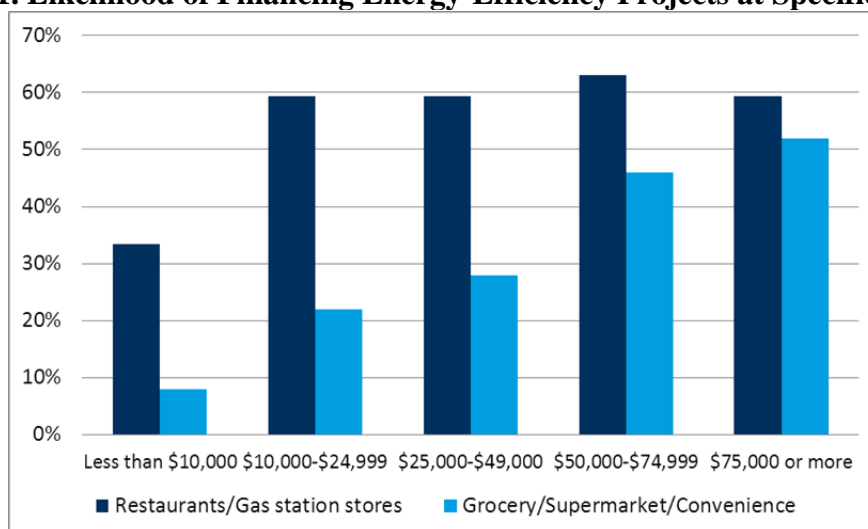
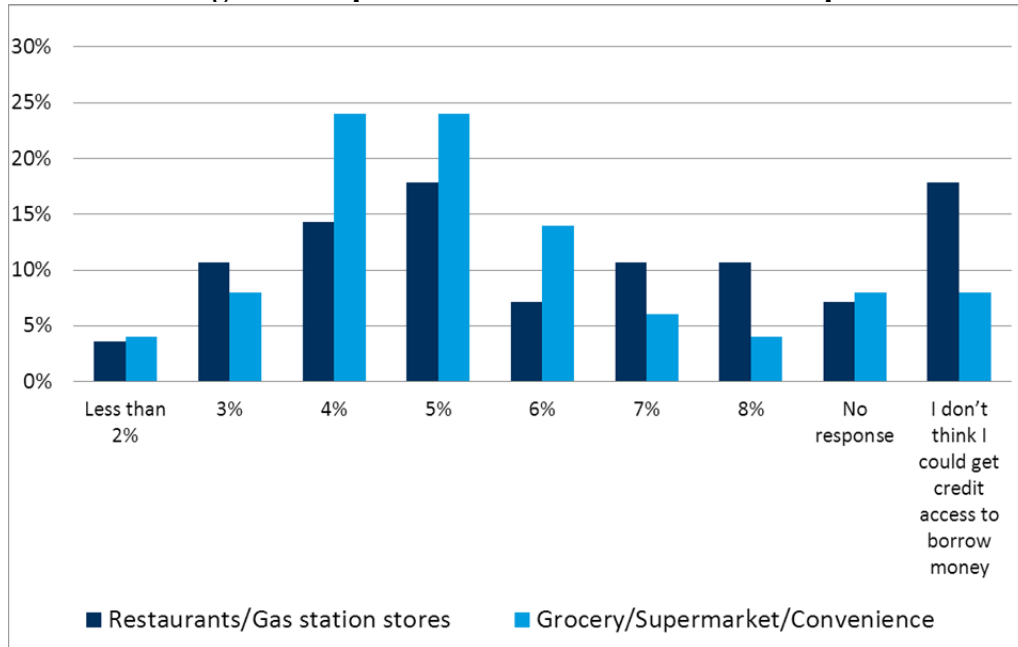


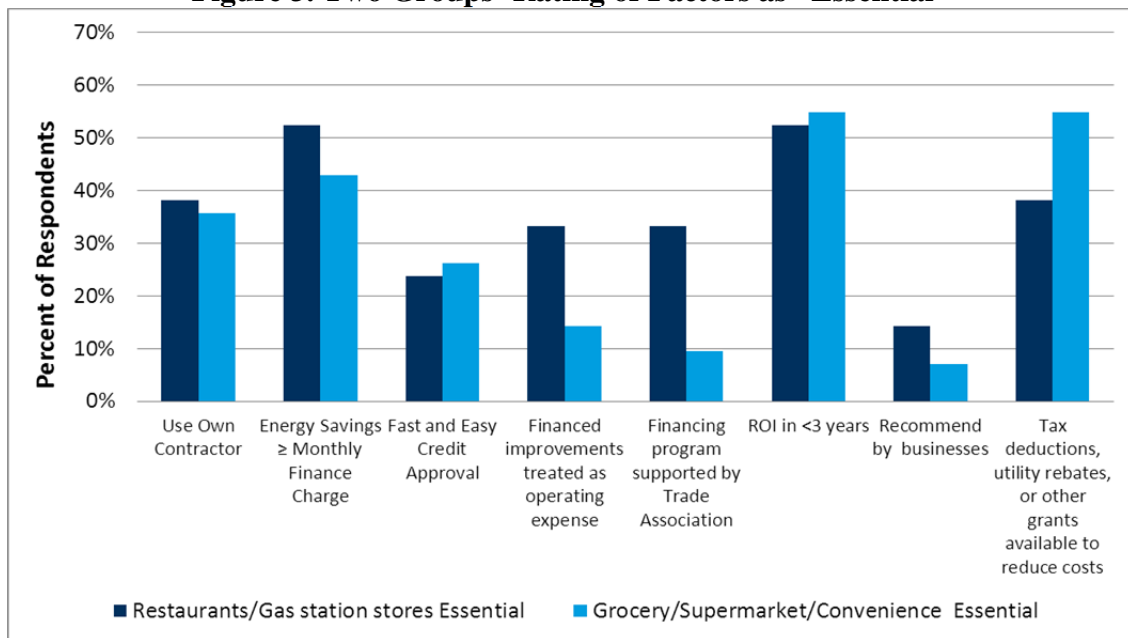
Figure 2 shows the current interest rates the two groups think they can get if they borrowed money today. Note that more restaurant and gas station mini-store owners (n=28) than grocery store owners (n=50) believe they cannot get credit access to borrow money at this time (18% vs. 8%). More restaurant and gas station mini-store owners expect interest rates of 7 or 8%.

Figure 2. Expected Interest Rates of Two Groups



The survey asked respondents to rate eight factors as *essential*, *preferred*, or *not essential*. Figure 3 shows the percent of respondents rating these factors as *essential* to a loan program (grocers: n=42; restaurants: n=21). The two groups responded similarly about using their own contractor, a return on investment of less than three years, and fast and easy credit approval. More restaurant owners stated it was essential that financing improvements be treated as operating expense, and that the trade associations support the financing program.

Figure 3. Two Groups' Rating of Factors as "Essential"



These three figures show the importance of understanding the issues relevant to the community and sub-communities in the target market. Segmenting the target market into smaller groups so there is flexibility to tailor the approach and messaging could build relationships, close more loans, and achieve greater energy-efficiency in this market segment.

Conclusions

Across the board, our research shows that the independent food vendor market is a hard one to reach due to its heterogeneity, geographic spread, unfamiliarity and inexperience with energy-efficiency opportunities and programs, lack of trusted relationships for program delivery, economic uncertainty, and narrow profit margins, among other challenges.

Our research also shows that target markets will need considerable attention, preparation, and ramp-up time if they are to take advantage of financing, even if interest is quite strong and savings are expected to be substantial. Awareness about and experience with energy-efficiency opportunities, benefits, and programs are low among the market's trade associations and their member businesses. Trust and relationships among market actors will need to be built. The right loan packages will need to be available or they will not pursue the financing or the energy-efficiency upgrades. Although some utility programs exist to provide additional financial support in some areas, most efficiency programs are not targeted specifically to this food industry sector. And, aside from the established utility rebate programs, contractors are not yet mobilized to deliver energy-efficiency services and financing opportunities to this sector.

We believe there exists a strong *community*—whether based on family ties, ethnicity, or shared business experiences and anchors—within the grocery sub-sector, which suggests it is the most ready for a loan program. This sub-sector responded most strongly to the trade association survey and voiced interest in energy-efficiency financing assistance, especially if coupled with other financial support such as utility incentives. Our secondary research also suggests that savings in the grocery sub-sector is likely to be the most substantial among the sub-sector on a per-store basis since improvements include significant refrigeration loads plus lighting and heating. To achieve these savings, we need to identify what attributes invite the concepts of energy-efficiency most deeply in this sub-sector, to find the loan package that is attractive and acceptable, and craft the messaging that resonates with this sub-sector.

Lastly, trade associations proved to be a critical component in reaching businesses in the grocery sub-sector, helping to design an attractive loan product and remaining involved as the loan products are formalized and marketed. Trade associations are known and trusted entities and can be a willing direct line to reach a variety of customer segments. Their primary purpose, after all, is to help their members succeed. We believe that such partnerships with trade associations can be made in other market segments.

By working together, the utility energy-efficiency programs, the commercial energy loan products, and building community relationships contribute to a more energy-efficient future.

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Appendix: Online Survey Questions

The online survey included the following questions.

1. How likely are you to make capital improvements of any kind at your business in 2012?
2. How likely is it that any of these improvements would include equipment or improvements that could save energy, such as lighting, refrigeration, HVAC, food preparation, insulation, windows, etc.?
3. How likely would you be to finance a capital expense at each of these levels? (circle one)

Less than \$10,000	Likely to finance	Not likely to finance	Don't know
\$10,000-\$24,999	Likely to finance	Not likely to finance	Don't know
\$25,000-\$49,000	Likely to finance	Not likely to finance	Don't know
\$50,000-\$74,999	Likely to finance	Not likely to finance	Don't know
\$75,000 or more	Likely to finance	Not likely to finance	Don't know

4. If you borrowed money today to finance improvements, about what interest rate do you think you could get? (circle one)
 Less than 2% 3% 4% 5% 6% 7% 8% 9% 10% or higher
 I don't think I could get credit access to borrow money
5. How willing would you be to use an experienced, licensed, and insured and authorized contractor, even if your usual contractor is not in the pool of contractors? (Third-party quality assurance would be provided to oversee the work of the authorized contractors.)
6. Let's assume you are interested in improvements to your equipment or building to save energy, and might consider financing. How essential would each of these factors be in your decision to finance the energy-saving improvements?

<i>How essential would each factor be in your decision to finance the energy-saving improvements?</i>	<i>Circle one answer for each</i>
a. You could use your own contractor to install the equipment.	Essential Preferred Not Essential
b. The energy savings would at least be as much as your monthly finance charge.	Essential Preferred Not Essential
c. Credit approval would be easy and fast (typically within 1 to 2 days).	Essential Preferred Not Essential
d. The financed improvements could be treated as operating expense instead of debt. For example, you could lease to own the equipment, and treat the lease as operating expense.	Essential Preferred Not Essential
e. The financing program is supported by your trade association.	Essential Preferred Not Essential
f. The savings on your bill would pay back your investment in 3 years or less.	Essential Preferred Not Essential
g. Other people in your line of business recommended the financing.	Essential Preferred Not Essential
h. You could get tax deductions, utility rebates, or other grants to help reduce costs of the improvements.	Essential Preferred Not Essential