

NASEO Financing Task Force Call Notes
Thursday, April 5, 2012; 3-4pm ET

Attendees:

OR	Energy Programs Consortium
GA	Chevron Energy Solutions
NY	Summit Energy Strategies
NC	Lawrence Berkeley National Laboratory
DC	MEEA
MI	JCI
NC	NASEO
IL	AHRI
Efficiency Maine	

Welcome and Introductions

Jeff Pitkin, NYSERDA

Jeff Pitkin, Treasurer of NYSERDA and Chair of the NASEO State Energy Financing Task Force, opened the call and introduced the topic of commercial property assessed clean energy (PACE).

Jeff also provided an update on NASEO's financing program activities. NASEO is starting an analysis study on innovative best practices in state energy financing programs. NASEO will be convening an Advisory Group of states and private sector partners to help guide this work. If you are interested in participating or would like more information, please contact Diana Lin (DLin@naseo.org).

Overview, Barriers and Best Practices of Commercial PACE

Mark Zimring, Lawrence Berkeley National Laboratory

[See presentation slides online.](#)

Mark provided a status update of commercial PACE across the country.

Once authorization for PACE is passed at the state level, it's up to the local community to design the program and create an opt-in option for participants. At this point, a program administrator will set up program standards and identify the financing structure and source(s) of capital. Of the PACE programs around the country, the largest difference between these programs is where the financing comes from. We've noticed that programs are now shifting toward the hybrid model.

Several program models currently being used or explored are:

- The Warehouse Model – the benefit is that it is incredibly simple and streamlined. However, in some places, like Sonoma County, we've noticed a challenge with the county having to hold funds while they wait for projects. We've also observed challenges with programs that have a set interest rate for all participants. A set interest rate is not very beneficial to commercial entities with good credit.
- Pooled Bond Model (as seen in Boulder County) – In these programs, a bond is issued once a significant amount of applications is received. Again, in this model we see the one rate for all participants which, again, may not be attractive to commercial entities with good credit.

- Open Market Model – One of the benefits for the Open Market Model is that it allows building owners to develop projects that fit their schedules, budget, and need. The downside here is that the transaction costs are quite high.
- Hybrid Models – [Ygrene](#) is one of these companies that is using a private line of credit to aggregate projects. They then look to the secondary market to leverage the take-ups of those aggregated projects.

PACE is still in early stages and there are only 10 programs currently operating and very few projects actually financed. Slide 7 shows the total number of projects that have been financed. Project sizes have ranged from \$5,000 to \$12M. In general, it's taken many programs a long time to launch.

Some of the challenges with PACE:

- Long program development cycle and high start-up costs. There is a need for significant deal flow (a lot of applications or projects ready) to make the economics of program setup work.
- Mortgage holder consent/acknowledgement requirement. Because PACE obligations hold a senior position and in the case of default the mortgage holders may not be made whole, mortgage holders are reluctant to give consent. Getting consent from the mortgage holder has been a big challenge for many. In cases where the building owner has a good relationship with the mortgage holder (e.g. a bank), they have been able to get consent more quickly.
- The Office of the Comptroller of the Currency (OCC) has recently [issued a statement](#) about the concern over commercial PACE, which creates some regulatory uncertainty and is making some lenders hesitant.

Q&A/Discussion

1. Is the Pooled Bond Model similar to a sustainable energy utility model, as seen in Delaware?
 - ✓ Answer: Delaware is operating a PACE program in addition to a utility program, but there is no reason that a utility couldn't run a PACE program. If they could go out and raise the funds, then the assessments could be financed using PACE.
2. Dave Good (DC) – From the Commercial PACE update table, can you tell us how many projects were funded through private capital?
 - ✓ Answer: Sonoma has done several projects – with just over \$1M in private capital. In Boulder they issued revenue bonds, but those were separate. In Minnesota there is an open market (or 3rd party financing). All in all, I'd say there's only a couple million in private capital across all of currently operating programs.
3. Mark Wolfe (EPC) – How are buildings that rely on natural gas using PACE?
 - ✓ Answer: A lot of these programs don't include the savings-to-investment ratio as we saw in other energy efficiency projects. Natural gas is more ubiquitous in the residential PACE programs – much more so than in commercial.

D.C. Commercial PACE Program

Dave Good, Government of the District of Columbia

[See presentation slides online.](#)

Dave Good works in the DC Dept of Environment's Energy Group and part of his work involves the development of DC's commercial PACE program. DC is still in the design phase of the program. DC is pursuing more of a Warehouse model. Dave presented on why DC decided to launch a commercial PACE program and how they designed it.

DC defines ‘success’ as a program that is scalable, market based (is neutral in terms of cost to DC), and can achieve the policy goals of the District (environmental health, energy security, economic development). The DC PACE program is also designed with those objectives in mind.

The pros and cons of PACE (Page 2 of presentation)

Pros: Scalable, Market-based, Affordable, Effective

- PACE can help to spur investment in energy efficiency and increase the number of energy efficiency upgrades and installations in commercial buildings. PACE addresses the top barrier to pursuing energy efficiency: available capital.

Cons: Complex, Unproven, Limited Scope, Lender Consent Challenge, Limited Interest from Capital Providers

- PACE has a limited scope right now because it’s a market-based approach and investors are hesitant to take on risk. DC wants to design a program that can eventually reach those buildings that offer greater risk / investment.

Why did DC decided to establish a PACE program? (Page 4 of presentation)

Capital: The availability of capital was a primary concern and PACE offered a way to provide capital at an affordable rate. Right now, DC is strapped for funds and is very hesitant to issue new debt. In 2009, DC used grant funding to design this program. PACE was also deemed to be the structure with the best ability to attract a large amount of private capital. DC anticipates \$70-\$100M of PACE assessments per year within the next 3 to 5 years.

Good Fit: The DC real estate market seems to understand PACE. Currently there is a mandate that the U.S. General Services Administration, one of the largest tenants in DC, needs to lease space that is energy efficient, and this is a huge driver for the program. Most of the projects in the pipeline are located in business improvement districts – which have helped DC target the program’s marketing efforts. Energy efficiency helps to improve property values in those areas. DC has green building code updates coming soon and that will also give regulatory support for the program. Other pending energy efficiency mandates will also require more energy efficiency buildings in the district.

Dedicated Leadership: Leadership through local and federal government, businesses and NGO’s in DC has helped to push this program forward.

Is Commercial PACE a Good Solution for Your State or Municipality? (Page 5 of presentation)

The support you have and timing is critical. What DC heard from the capital market is that the program needed to offer a market large enough to support at least \$50M to \$100M in PACE assessments each year. Lenders want to know that this program can be scaled up quickly. A regional PACE program may be a good idea in terms of gathering a lot of projects together, especially if you don’t think your area will be able to offer a large number of projects each month. If energy efficiency is not a priority for your state/ municipality, then maybe PACE is not appropriate for you right now. Right now, we’re seeing underwriting for credit worthy buildings – if you don’t have a lot of those, PACE might not be right solution for you either at this time.

PACE Enabling Legislation (Page 6 of presentation)

In DC it was very important that any PACE assessments were not back-stopped by any type of obligation to repay by the district (i.e. no general funds were to be used for the assessments). DC’s legislation requires acknowledgement but not mortgage holder consent (Although, the DC PACE Program has decided to require lender consent). It is important to structure your PACE program in a way that will be attractive to a capital provider. Don’t reinvent the wheel – there are 27 states with enabling legislation from which to learn from and adopt.

Factors to consider when selecting a contractor (Page 8 of presentation)

- Do you want to hire a contractor to design the program for your or will you design the program in-house? Most states will not have the capacity or necessary skills to fully develop a PACE program in-house.
- DC chose to hire a contractor with specific knowledge and experience to design a PACE program that would be attractive to borrowers and lenders. You need to find experts in the real estate market that you're trying to target. DC chose the contractor with the most commercial real estate experience. Of secondary importance was finding a team with a good understanding of capital markets and how they work – specifically commercial mortgage lenders. DC also evaluated the teams' project development, marketing capacity, size, and experience with public-private partnerships. Reference the RFP and find more information on DC's PACE Program on [NASEO's Energy Financing Resources Page](#).
- This particular program does require high administrative / start-up costs. We are paying for the design through ARRA funds, but once that is complete, the program administrator will only be paid through project fees.

Key Design Elements (Page 9 of presentation)

1. Simplicity – application process, eligible measures, measured savings
 2. Transparency – what the costs are, where the money goes and how it's being spent
 3. Cost – competitive with internal cost of capital, credit enhancement
- It's also important to look at other building upgrade measures that could be eligible under a PACE program – like water, or hurricane retrofits (as in FL). Think creatively to create a PACE program that fits your state/community's needs.
 - The message from property owners is: Offer a competitive option. DC is looking at an interest rate around 6% to be competitive in this market. DC is also considering credit enhancement as part of this program.

Who should be involved in the design process? (Page 10 of presentation)

- Building owners – what are needs, constraints, etc.
- Contractors – a wealth of knowledge
- Capital providers
- State and City Offices – other departments and programs (finance, tax and revenue, workforce, legal, etc.)

Q&A/Discussion:

1. Jeff Pitkin (NYSERDA) – Did I hear correctly that your program is requiring lender acknowledgement, but not consent?
 - ✓ Answer: DC's enabling legislation are requiring lender acknowledgement for assessments, but lender consent for projects.

DOE Financing Information Update

Rima Oueid, U.S. DOE

Rima Oueid, U.S. DOE, provided a [spreadsheet that serves as a companion to DOE's financing guidance](#). In addition, DOE's Financing Update is available online by visiting: <http://www.naseo.org/resources/financing/guidance/index.html>

Upcoming Calls:

The next call is scheduled for Thursday, May 3rd 2012 from 3:00 – 4:00pm ET.

The Task Force also holds regular calls on the first Thursday of every month from 3-4pm ET. Please visit the [NASEO State Energy Financing Task Force](#) page for information on past calls.