BETTER BUILDINGS
U.S. DEPARTMENT OF ENERGY

# BetterBuildings
# Financing Peer Exchange Call: *Commercial PACE*
## *Call Slides and Discussion Summary*

May 26, 2011

# Agenda

- Call Logistics and Attendance
- Commercial PACE Overview and Implementation:
  - Mark Zimring, Lawrence Berkeley National Lab
  - Wisconsin BetterBuildings program
- Questions and Answers
- Proposed Future Call Topics

# Participating Grant Programs

- St. Lucie County, FL
- New York (NYSERDA)
- Toledo, Ohio
- Madison, WI
- Maryland
- Connecticut

# Update on Commercial PACE Programs

**Mark Zimring**
**Lawrence Berkeley National Laboratory**
**Better Buildings Peer Exchange 26, 2011**

# PACE Financing Basics

## Government Sponsor

Upfront Capital

Repaid on
Tax Bill

## Property Owner

- Creates financing district & approval process
- Attaches repayment obligation to the building via property taxes
- May provide upfront capital

- Identifies work & chooses contractor
- Repays financing as a line item on the property tax bill (typically over 5-20 years)
- Repayment obligation transfers with ownership

# Impact of PACE Assessment

- **Creates a must-pay line item expense for owner.** The lien is senior to private liens and pari passu with other property taxes.
- **Results in a lien that is very secure.** Debt of property, not owner and de minimis to property's overall value.
- **Robust protection for existing lenders.** Mortgage holder consent/acknowledgement is required.

# PACE Financing Structures

1. **Warehouse model.** Government program sponsor uses a credit line (or internal capital) to fund projects, followed by ‘takeout financing’ (Sonoma County, CA).

2. **Pooled Bond model.** Government program sponsor aggregates project applications and then issues a bond to fund all projects at the same time (Boulder County, CO).

3. **Owner-arranged model**. Each owner negotiates financing terms directly with an investor. Government program sponsor issues bond to investor and passes through assessment payments to investor.

# Commercial PACE Benefits

- **No or Low Upfront Costs.** Removes high first cost barrier to investment.
- **Overcomes Credit Issues.** Provides investors with repayment security through priority of tax lien
- **Minimizes "holding period bias".** Assessment stays with the property, not the owner
- **Addresses "split incentives".** Property tax assessments may qualify as "pass-through expenses"

# Commercial PACE Challenges

- **High Legal and Administrative Setup Costs.**
- **Need Significant Deal Flow.** May not be appropriate for small towns and cities as scale is required to reduce costs (regional/statewide models can help).
- **Mortgage Holder Consent/Acknowledgement Required.** Buildings with mortgages in CMBS will likely not get consent.
- **Regulatory Uncertainty.** The OCC has expressed concern about commercial PACE.

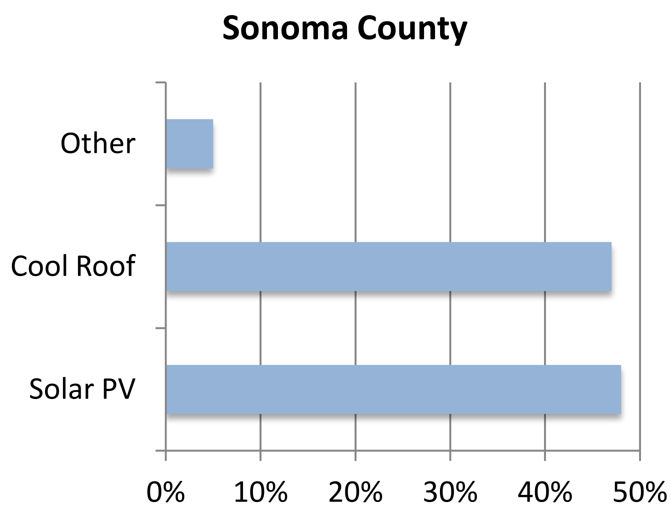
# Existing PACE Programs

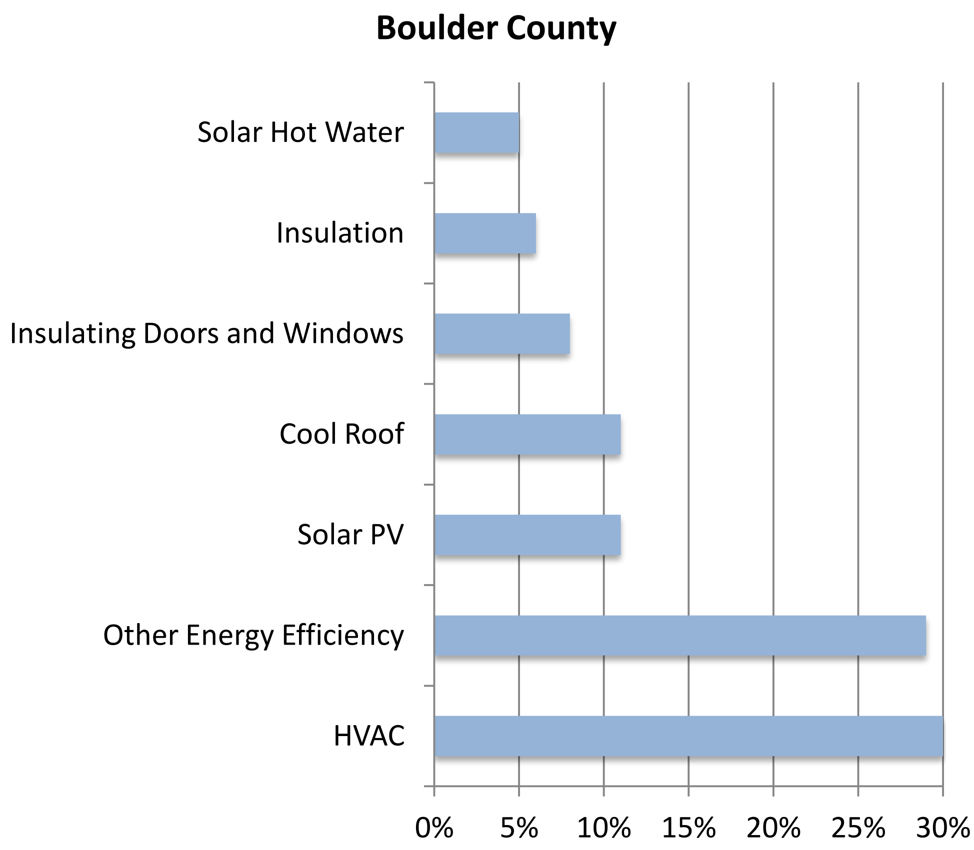
## Details of the 71 Approved Projects as of January 2011

| Program | Approved Projects | Total Approved Funding | Ave Project Size | Interest Rate | Term (yrs) | Funding Source |
|---|---|---|---|---|---|---|
| Sonoma County, CA | 37 | $7.3mm | $196k | 7% | Up to 20 | County Treasury |
| Boulder County, CO | 29 | $1.5mm | $51k | 1.04% or 2.29% | 5 or 10 | Moral Obligation Bond Issuance |
| Placer County, CA | 2 | $319k | $160k | 7.25% | Up to 20 | County Treasury |
| Palm Desert, CA | 3 | $575k | $192k | 7% | Up to 20 | City Backed Funds |

# Existing PACE Projects

## % of Approved Project Funding by Project Type



# Questions?

**Download the Commercial PACE Update Policy Brief Here:**

**http://eetd.lbl.gov/ea/ems/reports/pace-pb-032311.pdf**

**This Policy Brief Was Co-Written By:**

RENEWABLE FUNDING

CLINTON FOUNDATION | CLINTON CLIMATE INITIATIVE

BERKELEY LAB
Lawrence Berkeley National Laboratory

# PACE Strategies

## Best Practices and Lessons from the Field

Presented by

Todd Conkey
Energy Finance Development Director
WECC

# In the beginning…

- If not now, when?
- Fall 2009 Wisconsin State Statute (§66.0627) allowed for Special Charges through installments.
- Who will provide the capital?
  - Bond issuance was off the table at this point.

# What we did…

- Stakeholders
  - FI, property owners, City Treasurer, City Attorney, Outside counsel, City Appraiser, ESCO (JCI)
- Presentations
- Market interviews (+1MM sq. ft.)- 20 parties
- Expectations for rollout
  - Pilot borrowers and FI
  - Market voice to City
  - Passing of Ordinances in June

# What we found…

- Much discussion on why and what happens in worst case, i.e. foreclosure.
- How special charges/assessments are trued up with the County.  Can create liability.
- Not everyone upgraded for Y2K…
- FIs at this stage are not concerned, relatively speaking, of losing money.
- Owner-occupied are not that interested.  Capital competition.
  - FIs want owner-occupied deals now so this could pose a problem.
- No one wants riders or having to renegotiate leases.

# Our Product (draft until passed Ordinances)

- FI funded, more than likely first mortgage holder.
- Focus will be investor-owned property with triple-net leases.
- Application fee to program (~25 bps).
- Three-party agreement for Madison and Racine. Milwaukee will have blanket approval based on certain criteria placed in loan documents.
- Cash flow positive from day one.
- First Lien position in Madison and Racine. It will vary in Milwaukee
- Madison and Racine may assign collection rights to lenders. Milwaukee will assign collection to lender.
- Minimum size $10,000.
- Cash collateral product will probably also be utilized in conjunction.

# Hurdles and Solutions-PACE

| Hurdle | Solution |
|---|---|
| No capital | Funding from private lenders |
| Staff and system limitations | Aggregator of work and reporting |
| Understanding of PACE | Educate- presentations, case studies, documentation, legal opinion |
| Is it a Public Good?  Free market. | Educate- split incentive resolved, occupancy rates, NOI, collateral and property values |
| Sustainability | Application fee |
| Why? | Reasons for all:<br>•Muni- GHG, inventory, business flight<br>•FI- collateral, assignment of rent, NOI, Cash collateral<br>•Borrower-split incentive, NOI, improved occupancy |
| Borrower cash flow versus property | Probably our model |

# Questions and Answers

***How does a third party funding model work?***

The Wisconsin program is using a third party owner-arranged financing model. The capital will be coming from local financial institutions to fit a model where there is a relationship between a borrower and its bank. The financial institution could be a small, regional, or even a national bank.

***How much does it cost to set up and operate a Commercial PACE program? Can it be cost-neutral to local governments?***

For WECC, there was a $20,000 to $30,000 outlay to get the program going. It was money well spent. There currently is no information on the operating costs. Regarding cost neutrality, there is an application fee that goes to the program. The program is looking to charge a 1% origination fee and are evaluating other ways to create a revenue stream. When the grant period is over, this will all result in credit enhancements to the market; absent defaults, all of this money will be paid back.

# Questions and Answers

***Why did WECC choose its particular approach to Commercial PACE?***

There was never enough incentive for banks to do PACE transactions. The goal was to go deep into the market to provide options for people that were struggling with financing issues and to be able to come into the market with the cash collateral piece to get better loan tenors.

***What types of financial institutions are participating—commercial banks, credit unions?***

Based on Jacksonville, Florida's outreach it will probably be more local and regional institutions—all the way down to smaller community banks. It will depend on the type and size of clients seeking financing.

# Questions and Answers

***How does the Wisconsin approach compare to other Commercial PACE models?***

Wisconsin is doing a hybrid approach to PACE. The program is relying on seniority of the lien as a tax assessment in the event of nonpayment. But, it is minimizing the burden placed on local government by not requiring them to be part of the ongoing maintenance and servicing of financing. It is an interesting model.

The cities were interested in minimizing their workload. We still don't know what kind of volume they will see.

# Questions and Answers

***Does anyone have experience with Ygrene Energy Fund, which is working with Barclays Capital as a third party?***

They are working in the Miami-Dade County corridor in Florida. They are using a warehouse model and are charging 7%; all upfront costs are done by them.

They seem to be garnering attention in Florida and a number of other areas. They are looking to work in a few places in California. They have a potentially promising model, but there isn't much experience with implementation yet. They essentially cover the cost of the program. If you sign up with them, you get a "program in a box." Your only role is assessment and passing repayments to them through agents.

# Questions and Answers

**Is it wise for a local government implementing a Commercial PACE program to use its own collateral like a bank (similar to a revolving loan fund)?**

WECC's concern in taking that approach was that it didn't seem like a good way to get leverage.  With a $1 million revolving loan fund replenished by repayment of loans, it might take 5 years to get enough funds back to have financing to redeploy into the market.

# Proposed Future Call Topics

- Overcoming and Adapting to Financial Strategy Challenges
- PowerSaver Strategies
- Financial Product Messaging and Communications