



Strategies for Passing Property Assessed Clean Energy (PACE) Enabling Legislation

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Introduction to PACE

Legal Framework for PACE

Concerns & Solutions

Coalition Building: Minnesota Case Study

Resources for PACE Advocates



Introduction

What is PACE?

- **Definition:** PACE is a program designed to allow property owners to install small-scale renewable energy systems and make energy efficiency improvements to their buildings and pay for the cost over its functional life (e.g. 20 years for solar PV) through an on-going assessment on property tax bills.
- **PACE Innovation Removes Two Hurdles for Energy Retrofit Finance**

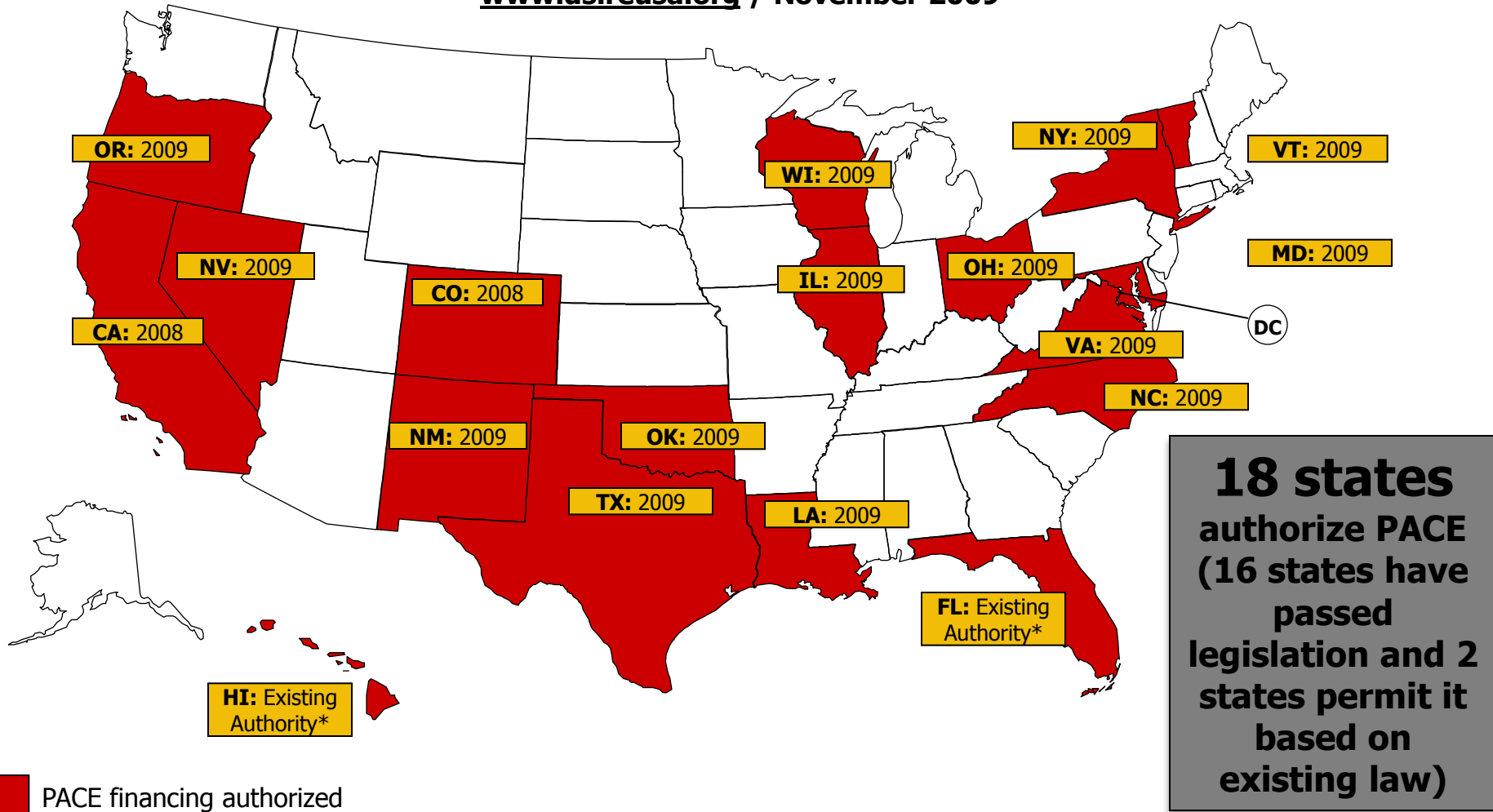
Hurdle

PACE Solution

- | | | |
|---|--|---|
| • Up-front cost to property owner |  | No up-front capital payment by property owner |
| • Risk that retrofit cost is not recouped upon sale |  | If the property is sold prior to the end of the repayment period, the new owner takes over the remaining payments as part of the property's annual tax bill |

Property Assessed Clean Energy (PACE)

www.dsireusa.org / November 2009



Legal Framework for
PACE

PACE is simply an expansion of traditional land-secured financing

Steps in Land-Secured Financing

Local government approves financing of improvement with a defined public interest, such as a park or sewer system.

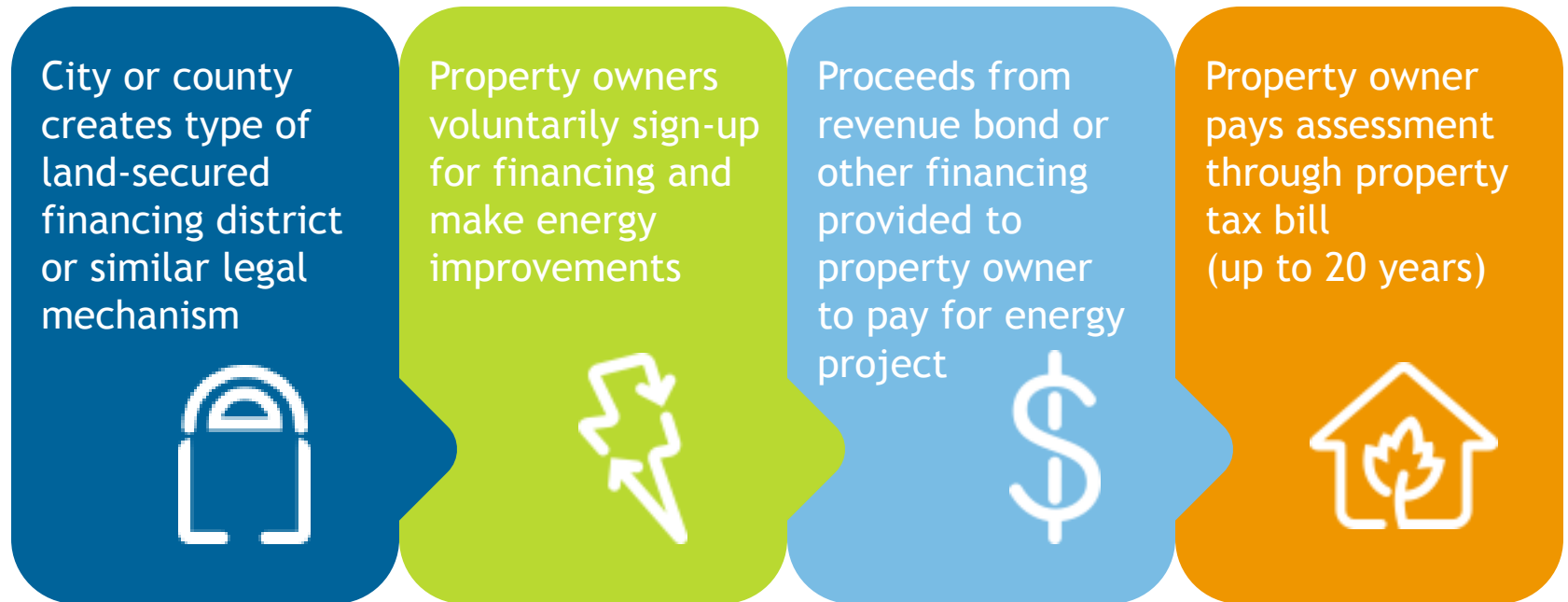
Costs for the improvement are identified and local government issues bond to pay up front capital costs.

Senior assessment or tax lien placed on properties that receive a benefit from the financed improvement.

Lien secures assessment levied on benefitted properties through property tax bill. Assessment repays bond investors.

*** Land secured financing districts – variously referred to as assessment districts, public improvement districts and community facilities districts – are a familiar tool of municipal finance. They are used to finance projects which serve a public purpose, including street paving, parks, open space, water and sewer systems, sports arenas and street lighting, among others.*

How PACE works



** Unlike traditional land-secured financing, PACE programs are 100% voluntary -no property owner pays additional assessments or taxes unless they choose to have work done on their property. Program participants pay only for the cost of their project (including interest) and nominal fees to administer the program.

The Berkeley FIRST Model

- Existing authority: Mello Roos Community Facilities Act
 - Assessment mechanism
 - Bonding authority
- City of Berkeley's Amendments to provide for PACE:
 - EE and RE as allowable purposes of district
 - Permissible on publicly or privately owned property
 - Opt-in mechanism
 - Legislative findings of valid public purpose
- Results of pilot program: financed ~ 40 residential solar & energy efficiency projects

Key Features of PACE Legal Authority

- Local government finance authority
- Local government assessment mechanism
- Energy efficiency and renewable energy as allowable improvements/projects
- Authority to finance improvements on private property (residential, commercial, industrial)
- Voluntary participation via opt-in mechanism
- Legislative findings that financing has a public purpose
- Assessments secured via lien on the property
- Local government bonding authority
- Authorization for multijurisdictional programs
- Authorization to accept federal & state grants and loans

Concerns & Solutions

1. PACE is not a new type of financing

PACE is a form of land-secured financing districts which have a 100+ year history in the U.S. to pay for improvements in the public interest*

PACE finance public purposes include: Energy efficiency & renewable energy goals, greenhouse gas reduction, global climate change mitigation, advancement of clean energy economy, and improved energy independence

- Local governments have a long-established right to levy assessments to pursue a valid public purpose
- 37,000 land-secured districts exist in the U.S. and are part of the standard mortgage underwriting process
 - Referred to as improvement districts, assessment districts, etc. and used to finance wide range of improvements with public and private benefit (streets, sewers, street lighting, etc.)
 - Many historical examples of “voluntary” property-by-property land-secured financing districts across the country (seismic – CA; septic replacement – MA; sidewalks - NJ)
 - *Dressman v. Farmers' & Traders National Bank of Covington*

*See *Bloomberg Law Reports* article on PACE Land-Secured Districts ([click here](#))

2. PACE Programs create value for the mortgage lending industry

*Properly designed PACE finance programs actually **reduce risks and provide value** for existing mortgage lenders.*

- **Clean energy improvements raise property values**
Appraisal Journal found a \$1,000 annual reduction in utility bill will raise property value \$20,000
 - Study found “green certified” homes sold for 5-10% more than similar homes without energy improvements
- **Lowering energy bills decrease risk of default**
 - Because participating property owners’ utility bills will decrease, funds will be freed up that can be directed towards other obligatory payments, such as a mortgage payment.

3. PACE programs do not impair mortgages

- **Even in a Worst Case Scenario Impairment of Existing Mortgage is Negligible:**
 - If homes with PACE assessments are foreclosed, in most states, the mortgage holders would have to repay the County only the back tax lien payment. This is because in a foreclosure, most state laws provide that the assessment lien is not ‘accelerated’ at foreclosure or transfer. Only delinquent assessments are due, not the entire lien. The next property owner will inherit the remainder of the PACE assessment.
 - Thus even if 10% of PACE homes in a portfolio went into foreclosure (national foreclosure rate is under 5%) with an average \$20,000 lien, **the average loss to the mortgage holder would be \$170 per property.**

4. Federal PACE 'Framework' protects consumers and lenders

- **White House Policy Framework on PACE Underwriting Criteria Developed in Oct, 2009.**
 - Federal government created standard underwriting and project screening criteria for PACE programs. DOE administers.
 - Framework approved by White House, Treasury Department, Department of Housing and Urban Development, Department of Energy , and others.
 - [http://www.whitehouse.gov/assets/documents/PACE Principles.pdf](http://www.whitehouse.gov/assets/documents/PACE_Principles.pdf).

White House Framework

Property owners must meet strict guidelines:

- Ensure that the property is not in distress (ie, all mortgage payments/property taxes are current, and there aren't any conflicting liens)
- Limit the maximum lien value to a specific percentage of the property value.
- Limit financing to property owners that meet a minimum equity threshold.

Projects must meet strict guidelines:

- Limited list of eligible energy reduction measures appropriate to that community
- Must meet cost-effectiveness standard
- Required third-party quality assurance program

White House Framework

“In sum, PACE programs have the potential to increase the accessibility and affordability of energy saving measures, consequently lowering energy bills to residents and reducing the environmental footprints of participating localities. If programs are not properly constructed, however, the programs could potentially create risk for homeowners and lenders. Adoption of best practices, including strong contracting standards in the selection of those doing the retrofits, will help deliver the type of market transformation we need to see retrofitting scale up and achieve our goals. “

– White House Policy Framework on PACE

5. Property owners do not add to debt burden of property owners

- The purpose of credit checks and debt-to-income analysis is to ensure that property owners do not take on debt they cannot afford.
- PACE accomplishes the same goal through other means:
 - Ensures properties are not “underwater” on their mortgage, are current on property taxes, etc.
 - Limits projects to those that meet a cost-effectiveness test so that property owners have increased cash flow from their utility bill savings to cover the assessment payments

6. Banks and lenders can (and do) participate in PACE programs

- Banks are engaged in PACE programs across the country.
 - Providing interim and long term finance
 - Purchasing PACE bonds
- PACE programs increase demand for energy efficiency and solar projects, many of which are financed through traditional financing sources, such as a home equity line of credit.

*Coalition Building:
Minnesota Case Study*

Building a Strong Coalition: Minnesota Case Study

Starts With a Focused Plan

- Analyze Strengths and Weaknesses
 - Engaging Potential Supporters
 - ✓ Cities/Municipalities
 - ✓ RE/EE Businesses
 - ✓ Labor
 - ✓ Environmental Orgs
 - Engaging Potential Opponents
 - Mortgage companies, realtors, auditors, utilities

Open Dialogue and Communication is Key

Building a Strong Coalition: Minnesota Case Study

- Establish Strong Coalition to Hit each Message:
 - **JOBS:** Minnesota Solar Energy Industry Association (Lynn Hinkle), Minnesota AFLCIO (Jobs Coalition)
 - **ENVIRONMENT:** Institute for Local Self Reliance, Izaak Walton League (Jenny Meyers), North Star Chapter of Sierra Club (Justin Faye) and Fresh Energy (Linda Taylor), Solar Cities.
 - **DEMAND from CITIES:** League of Cities

Building a Strong Coalition: Minnesota Case Study

- Build Movement Quickly
- Mobilize Constituent Support
 - Letters/emails
 - Testimony for Committee Hearings
- Be Ready to Counter Your Opponents
 - Vote Solar/PACENOW.org Resources
- Have Fun!

*Resources for PACE
Advocates*

PACE Summary

- PACE is an innovation that solves the financing problems associated with energy efficiency & retrofit investments
- PACE finance districts are based upon long established history of “land secured financing districts”
- PACE benefits virtually all stakeholders, including homeowners and existing lenders, while creating large job growth and all with no credit risk to municipalities
- PACE enabling legislation has been adopted by 16 states in little more than a year
- PACE has broad support from: The White House and major federal agencies, U.S. senators/congressman, bipartisan states/governors/mayors and other state leaders, large unions, NGO’s and major corporations
- PACE had initial concerns raised in mid-2009 by the mortgage and housing industries which were cured by:
 1. The work of The White House Inter-Agency PACE Task Force and the PACE White House Policy Framework it published in late 2009
 2. Municipalities around the country incorporating the “Best Practices” outlined in the PACE White House Policy Framework
- The PACE Best Practices Framework that is being implemented results in benefits to existing lenders, including:
 - Improved credit profile: Reduced risk of borrower default due to increased cash flow (savings>tax payment) & increased collateral value
 - Immaterial PACE lien seniority because lien does not accelerate: Seniority in foreclosure is less than \$200 on a portfolio of homes ([click link](#))
- PACE senior lien status is mandatory both from a legal perspective as an assessment and from a practical perspective of administering assessments and marketing bonds (click on [Barclays Capital Memo](#))
- PACE has the potential to dramatically accelerate the energy retrofit of our nation’s building stock

PACE Supporters

Federal:

- White House Inter-Agency Task Force (Treasury, NEC, HUD, DOE, OMB, FHFA)
- Vice President Biden – Announcement at “Recovery Through Retrofit” Conference
- Secretary Chu – Announcement at “Recovery Through Retrofit” Conference
- Secretary Donovan – Announcement at “Recovery Through Retrofit” Conference
- Senate Leaders – Support letter for PACE sent to President Obama from Senator Bingaman, Chairman, Committee on Energy & Natural Resources, and 7 other senators

Click on Link:

- [Inter-Agency PACE Report](#)
- [Biden YouTube Clip](#)
- [Chu YouTube Clip](#)
- [Donovan YouTube Clip](#)
- [Senator Letter](#)

States:

16 States have recently passed PACE enabling legislation, including:

- California
- Colorado
- Illinois
- Louisiana
- Maryland
- Nevada
- New Mexico
- New York
- North Carolina
- Ohio
- Oklahoma
- Oregon
- Texas
- Vermont
- Virginia
- Wisconsin

➤ Hawaii and Florida appear to have existing PACE authority

State Leaders:

Bipartisan governors, mayors and legislators across the nation endorse PACE (click here to see [Governor Schwarzenegger’s \(R\) announcement](#) and [San Diego’s Mayor Jerry Sanders’ \(R\) announcement](#))

PACE Supporters (cont.)

Organized Labor PACE Supporters:

- International Association of Heat and Frost Insulators and Allied Workers
- International Brotherhood of Teamsters
- International Union of Painters and Allied Trades (IUPAT)
- Laborers International Union of North America (LIUNA)

NGO PACE Supporters:

- Alliance to Save Energy
- American Institute of Architects (AIA)
- Americans for Clean Energy
- Bipartisan Policy Center
- Center for American Progress
- Center for Sustainable Energy
- Clinton Global Initiative
 - ([click on link for President Clinton's PACE Announcement](#))
- Environmental Defense Fund (EDF)
- Milken Institute
- National Association of Real Estate Investment Trusts (NAREIT)
- Natural Resources Defense Council (NRDC)
- Polyiso Insulation Manufacturers Association (PIMA)
- Real Estate Roundtable
- Sierra Club
- Solar Energy Industries Association (SEIA)
- Stewards for Affordable Housing for the Future (SAHF)

Corporate PACE Supporters:

- Johnson Controls Inc.
- Jones Lang LaSalle Inc.
- Masco Home Services
- ProLogis
- Siemens Corp
- Simon Properties Group
- Tishman Speyer
- Trane

Financial Institutions Working on PACE:

- Barclays Capital
- Citicorp
- Goldman Sachs
- Royal Bank of Canada
- Wells Fargo

PACE Resources

PACE Legislation Toolkit: Below items are helpful resources for state campaigns and for diffusing arguments made by mortgage banking industry:

Resources:

- PACE Finance: Benefits, Concerns & Solutions Implemented (check www.pacenow.org for link)
- [PACE Concerns & White House Solutions](#)
- [PACE Programs, Historical Precedent](#)
- [PACE Bloomberg Law Article on PACE Land-Secured Districts](#)
- [Template for PACE Letter to State Legislator](#)
- [PACE Letter Template to Legislator Which Addresses Lender/Consumer Concerns](#)
- [Template for State Legislation Coalition Petition](#)
- [The 10 Must Haves for PACE State Enabling Legislation](#)
- [Barclays Capital Memo – PACE Seniority is Mandatory](#)
- [“Recovery Through Retrofit” Report](#)
- [White House PACE Policy Framework/Best Practices](#)
- [VP Biden YouTube Announcement](#)
- [Secretary Chu YouTube Announcement](#)
- [Secretary Donovan YouTube Announcement](#)
- [Senator Letter to President Obama](#)
- [Consortium Letter to Congress](#)
- [Governor Schwarzenegger’s Announcement](#)
- [Mayor Jerry Sanders’ Announcement](#)
- [PACENOW Website](#)
- [Vote Solar Website](#)

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Appendix

Benefits of PACE Finance

Our Nation:

- Large job creation
- Very low fiscal cost & high probability of success
- Accelerates movement toward energy independence & reduces GHG emissions

Property Owner:

- Elimination of “up-front” cost barrier and risk that retrofit cost is not recouped
- Positive cash flow on retrofits (annual savings>cost) frees up household income for mortgage payments
- Lower energy bills and lower vulnerability to spikes in energy prices

States, Cities & Municipalities:

- Immediate job creation
- No credit or general obligation risk: Obligation is liability of real estate owner
- Greenhouse gas reductions/energy independence
- Opt-in: Only those real estate owners who opt-in pay for it

Existing Mortgage Lender:

- Improved credit profile/reduced risk of mortgage default due to increased homeowner cash flow. Positive cash flow on retrofits (annual savings>cost) reduces default risk
- Increased collateral value
- PACE senior lien in a foreclosure is de minimis: Less than \$200 per home on a portfolio of homes ([click on link](#))
- Lower energy bills means borrower has lower vulnerability to spikes in energy prices

PACE Lien Seniority Paid in Foreclosure is Immaterial: Less Than \$200 Per Home

Question: If property owners default on their PACE Payments, isn't the mortgage company left paying the bill?

Answer: There is no bill to pay. On a portfolio of homes, each with a \$250,000 mortgage, the PACE lien seniority in foreclosure amounts to less than \$200. This is due to three factors:

- Only Delinquent Assessments Are Paid: In most states, upon foreclosure only the delinquent tax lien gets paid (on average, 1 year of back tax payments not the whole PACE loan) while the new homeowner assumes the remaining balance
 - Our nation's foreclosure rate peaked at 10% and has averaged 5%
 - Small Percentage of Home Value: PACE retrofits are relatively small compared to home value (i.e. 5% - 10%)
- Thus even If 10% of PACE homes in a portfolio went into foreclosure (national foreclosure rate is under 5% subprime crisis peaked at 10%) with an average \$20,000 lien, **the average PACE seniority would be \$170 per property.**
- See detailed example on next page.

PACE Lien Seniority Paid in Foreclosure is Immaterial: Less Than \$200 Per Home (cont.)

Foreclosure Example:

Assume you have a \$300,000 home, \$250,000 mortgage:

- Assume the home has a \$20,000 (6% interest rate) 20 year PACE loan that is paid off \$1,700 per year for 20 years. If the house is foreclosed on with 1 year of PACE payments in arrears, then the 1 year of back payment - or \$1,700 – is paid ahead of the mortgage, not the full \$20,000. Note: Typical back payment in foreclosure is 1 year.
- So in this example, the mortgage has \$1,700 paid ahead of it. Far fewer than 10% of homes will result in foreclosure (10% is where the subprime crisis peaked). For conservatism, assume 10% of all PACE homes in the above scenario result in foreclosure.
- This suggests that with a "portfolio" of Fannie/Freddie mortgages that have PACE liens, the impact is 10% in foreclosure x \$1,700 one year delinquent lien or **\$170** (yes, \$170 per home on average). Realistically, probably less than 5% of homes would result in foreclosure, which results in an average **\$85** of seniority in foreclosure on the hypothetical portfolio of Fannie/Freddie mortgages.

The PACE lien increases the value of lender collateral during foreclosure:

- The above PACE seniority numbers assume no incremental sale value from the \$20,000 that was spent on the retrofit
 - The *Appraisal Journal* estimates that home values increase by \$20 for each \$1 in annual energy savings ([click here for article](#))
 - Assuming only fractions of this projected incremental value, existing mortgage lenders enjoy substantially more collateral coverage with the PACE retrofits – even in foreclosure situations

Senior Lien Mandatory Requirement for PACE Districts

PACE Finance requires senior lien status for a number of reasons:

- **Land-secured financing districts require senior liens to function programmatically and legally**
 - Virtually all municipal tax collection and disbursement systems are based on senior lien status of assessments
 - There are no mechanisms, municipal staff, nor bankruptcy laws in place to handle a junior tax assessment
 - There is no statutory authority for subordinate tax assessment liens in most states
- **Senior lien required for private capital**
 - Security of repayment compromised without lien seniority
- **See Barclays Capital Memo on Legal & Market Requirement of Seniority ([click here](#))**
- **Repayment obligation is attached to property, not person**
 - Senior lien allows for the repayment obligation to transfer between owners
 - Senior lien allows for long term repayment, matching life of energy improvement and allowing for positive cash flow to property owner

PACE Finance: Detailed Best Practice Chronology

Early 2009 - Concerns Raised:

- During the development of PACE Finance questions and concerns were raised, primarily from the mortgage banking and housing industries

Mid 2009 – White House Recognizes PACE Potential & Forms Inter-Agency Task Force:

- Vice President Biden forms White House Inter-Agency Task Force to Focus on PACE Acceleration & Best Practice Standards:
 - Inter-Agency task force comprised of senior officials from the Federal Housing Finance Authority, Department of Energy, Treasury Department, Housing and Urban Development Authority, and the Natural Economic Council

Fall 2009 – Vice President Biden Announces Launch of National PACE Initiative:

- Vice President Biden, Secretary Chu & Secretary Donovan announce PACE Finance as key component of our nation’s [“Recovery Through Retrofit”](#) program
- White House Task Force publishes [White House PACE Policy Framework & Best Practices](#) (“WH PACE Best Practices”) to cure banking and housing industry concerns

2010:

- Municipalities begin to incorporate [WH Best Practices](#)
 - San Francisco:** Our nation’s first major PACE program integrates WH PACE Best Practice’s (click on link - [SF GreenFinances Program Terms](#))
 - Small Municipalities:** Small municipalities, like Montgomery County, MD, embrace WH Best Practice Framework (click on link - [Montgomery County Program](#))
 - Future Program Launches:** Near-term program launches will benefit from WH Best Practice’s, including major launches throughout California (Los Angeles, San Diego, etc.), Louisiana, and New Mexico

WH Best Practices: Homeowner & Lender Protections

- **White House PACE Best Practices Objectives:**
 - Establish clear guidelines that support the acceleration of PACE nationwide
 - Protect consumers and minimize the risk to lenders and borrowers
- **Homeowner Protection Examples From White House PACE Best Practices:**
(click here for [WH PACE Best Practices Report](#))

Protection

Annual utility bill savings should exceed increase in annual tax assessment payments

PACE finance limited to high impact projects

Energy audits/licensed contractors/
quality assurance

Adequate consumer disclosure/training
for homeowners

Purpose

To ensure that the homeowner's cash flow increases so they have more income to make mortgage payments.

To ensure that retrofits are limited to projects that have well documented efficiency gains. This maximizes the impact of PACE on improving efficiency and protects homeowners and lenders.

These measures are meant to ensure that the homeowner's retrofit is constructed as intended. Municipalities should have the power to disqualify contractors who fail to remedy problems – strong incentive to complete work correctly.

To reduce the risk of consumer fraud.

WH Best Practices Homeowner & Lender Protections (cont.)

- **Lender Protection Examples From White House PACE Best Practices:**
(click here for [PACE White House Best Practices Report](#))

Protection

Annual utility bill savings should exceed increase in tax payments

Property value exceeds property debt

No current default by homeowner

Limit maximum PACE lien value to percentage of property value

Clear title

Purpose

To ensure that the homeowner's cash flow increases so they have more income to make mortgage payments and default risk decreases.

To avoid PACE loans to borrowers who have properties in distress as these borrowers are more likely to default. PACE programs should compare estimated value to outstanding debt.

To decrease risk by avoiding homeowners who are not current on taxes, have unsatisfied liens, have notices of default, or have any other material delinquencies.

Maximum lien percentage, such as 10%, ensure that PACE retrofits remains a relatively small percentage of overall home value.

To avoid easements, liens, subordination agreements, etc. that conflict with the PACE assessment.