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DATE: September 9, 2015

TO: Board of Commissioners

FROM: Patrick Quinton, Executive Director

SUBJECT: Report Number 15-55

Adopting the Commercial Property Assessed Clean Energy Program

BOARD ACTION REQUESTED

Adopt Resolution No. 7144

ACTION DESCRIPTION

These actions by the Portland Development Commission (PDC) Board of Commissioners (Board) will approve the establishment of the Commercial Property Assessed Clean Energy (CPACE) Program. If approved, the CPACE Program will allow PDC to provide loans to owners undertaking energy efficient retrofits of commercial buildings.

In order to establish PDC's role in the CPACE Program, staff requests that the PDC Board take two formal actions that will (i) establish Program Guidelines under which PDC can make CPACE Program loans, and (ii) authorize the Executive Director to execute an Intergovernmental Agreement (IGA) with Multnomah County (County) that will allow PDC to administer the CPACE Program on behalf of the County. On September 3, 2015, the County Board of Commissioners approved the CPACE Program and IGA.

PDC staff is proposing to test the CPACE Program through a two-year pilot, during which PDC and the County will monitor progress and make changes to the CPACE Program to better meet shared goals.

BACKGROUND AND CONTEXT

The City of Portland (City) and the County adopted the 2009 Climate Action Plan which established a goal of reducing local carbon emissions by 80 percent from 1990 levels by 2050, with an interim goal of 40 percent by 2030. The largest producer of carbon emissions in Portland and Multnomah County is energy used in buildings and industry, with 24 percent of Multnomah County's carbon emissions coming from electricity and fossil fuels used in commercial buildings. To achieve the 2050 goals, it is imperative to reduce the energy consumption of the commercial building stock. Energy improvements have the added benefits of fostering economic growth, creating jobs, and improving property values.

Oregon Revised Statutes 223.396, authorized in 2009 and amended in 2014, allows local jurisdictions to create CPACE financing programs. CPACE is an adaptation of a common financing technique used for decades throughout the United States: local government financing of local improvements that meet a public purpose, which is secured by a special assessment tax lien and repaid with a property tax assessment.

In 2012, JDM Associates (JDM) prepared a market study that identified strategies for PDC to develop energy efficiency programs and resources to cultivate and foster the energy efficiency market in the

Portland metropolitan area. In JDM's study, building owners identified a lack of financing tools as a significant barrier to undertaking energy projects, most notably deep energy retrofits that would achieve greater energy savings and reduce the region's carbon levels. The CPACE loan was recommended to PDC as a potential tool to address the lack of capital financing and stimulate more energy efficiency projects. Simultaneously, the County's sustainability staff was exploring the development of a CPACE program and reached out to PDC as a potential partner to help develop and administer a program using the County's property tax system as the security mechanism.

The County commissioned a study from EcoNorthwest in 2012 to evaluate the size of a CPACE market. PDC staff's analysis of that study along with data from CADMUS Group, a consulting firm, concluded that a sufficient market would benefit from a CPACE financing structure, and that PDC's primary CPACE market are buildings between 10,000 and 50,000 square feet. This market is large enough to generate adequate loan production to sustain the program over time.

CPACE STRUCTURE

The new CPACE financing mechanism uses the property tax structure to secure financing for energy improvements to commercial buildings under the premise that energy improvements provide a public benefit because of the environmental benefits achieved by reducing carbon emissions. The cost savings achieved by the improved energy efficiency of the buildings are used to finance the improvements. The loan is secured by a "benefit assessment" lien that has priority over all other encumbrances, other than regular property taxes. Existing lien holders must consent to the filing of the CPACE lien.

This financing structure addresses the principal market barriers to investment in energy efficiency and on-site renewable energy projects: lack of access to capital, short repayment terms when capital is available, lack of transferability of the debt, and the disconnect between who pays for the improvements and who benefits from the energy cost savings (known as the split incentive.)

CPACE offers commercial building owners (commercial, industrial, and multifamily residential properties with five or more units) up-front, long-term financing for up to 100 percent of the cost of energy upgrades; the financing is repaid with CPACE benefit assessment payments with a maximum term set at the average useful life of the energy upgrades. CPACE assessments attach to and follow title to the property. If the property is sold before the CPACE loan is fully repaid, the assessment remains in place and the repayment obligation is automatically transferred to the next owner. The senior lien status of a CPACE assessment substantially reduces the risk, making CPACE loans very secure and attractive to lenders and investors. In addition, because the benefit assessment is considered part of the property taxes, it can often be passed through to tenants in a triple net lease structure, thus linking the payment of the energy improvements with the party that benefits most from those improvements.

PROGRAM ADMINISTRATION

An element of the program design is to leverage the technical capacity of multiple organizations. The County will exercise its legislative authority to create the CPACE Program and execute an IGA with PDC to administer the program on its behalf. The CPACE Program will also leverage the technical expertise, existing energy audit, and trade ally infrastructure of Energy Trust of Oregon to facilitate energy audits on the buildings selected to participate in the pilot.

CPACE PILOT PARAMETERS

PDC staff is proposing that PDC and the County pilot the CPACE Program over the next 24 months and that it initially be tested in urban renewal areas (URAs) using tax increment financing (TIF). If approved, during the pilot PDC will originate a limited number of transactions (up to 10) under the terms and conditions outlined in the CPACE Program Guidelines and allocate up to $3,000,000 in Commercial

Property Redevelopment Loan (CPRL) funds from applicable URAs (for budgeted and forecast CPRL funds across URAs, see Attachment A). All PDC loans will follow existing PDC approval protocol including review by PDC's Financial Investment Committee.

The pilot program structure allows PDC and County staff to design, test, and refine various elements of the program, including:

- A long-term *capitalization strategy* to attract non-TIF resources to the program;
- Establishment of a *certified firm* strategy to provide contracting opportunities within the CPACE Program;
- A *marketing and outreach* strategy to drive loan production; and
- The *internal systems* to support a production model of lending and full integration of the program into PDC operating departments at completion of the pilot.

CERTIFIED FIRM SUPPORT STRATEGY

Both PDC and the County have strong commitments to advancing social equity by increasing economic opportunity for historically disadvantaged populations and creating equitable access to living wage jobs and wealth creation opportunities. The PDC 2015 – 2020 Strategic Plan identifies closing of equity gaps as a prime focus of PDC's resources and activities. Similarly, the PDC Equity Policy allows the use of one or more certifications of construction contractors to increase the utilization of firms owned by people from underrepresented to grow their capacity. These certifications include the federal Disadvantaged Business Enterprise (DBE), Minority Business Enterprise (MBE), and Woman Business Enterprise (WBE).

During the pilot, PDC and County staff will develop an approach that provides certified firms an early-entry advantage within the CPACE Program while taking into account that the availability of certified firms owned by underrepresented populations may be limited in today's booming construction economy, and that it is not possible to predict ahead of time what specific scopes of work will be involved in any given project.

Acknowledging these possible limitations, the framework of the strategy includes the following components:

- *Programmatic Goals*: There are a number of CPACE Program goals related to utilization, including the number of certified firms in the contractor pool that participate on projects, the number of diverse workforce participants, the number of projects brought to the CPACE Program by certified firms, the variety of firm size and experience in the contractor pool, and a comprehensive list of firms certified in the commercial building sector.
- *Certified Contractor Pool:* Develop a contractor pool targeted specifically to underrepresented certified prime and sub-contractor firms. Firms will meet a set of minimum requirements for participation. Certified firms will be linked to services (as necessary) to build capacity and establish a competitive advantage on CPACE projects. Services may include a line of credit to cash flow a CPACE project and assistance with business certification and licensing. Once the pilot is complete, PDC will evaluate the success of the CPACE Program as well as the degree to which certified firms have gained experience within the program to better compete within the industry.
- *Equity Advisory Group:* For the longer term, a working group consisting of prime contractors, subcontractors, and industry support organizations will be formed that will participate in goal setting for equity integration and to monitor progress, assist with outreach, and provide support services to the contractor pool.

Should the PDC Board approve the CPACE Program, PDC will convene a work group of stakeholders (including the National Association of Minority Contractors-Oregon, the Metropolitan Contracting

Improvement Partnership, Portland Chapter of the National Association for the Advancement of Colored People's Economic Development Committee, the Hispanic Metropolitan Chamber of Commerce and others) to identify the details and specific steps of creating the contractor pool and to determine the most effective steps to maximize the utilization of certified firms from underrepresented communities.

SUCCESS MEASURES

The success of the pilot phase of the CPACE Program will be measured by:

- Three projects at different stages are in the pipeline by the end of 12 months.
- Six loans are approved within 24 months.
- Four projects are complete or in construction at the end of the Pilot period.
- At least two private lenders have agreed to participate.
- DBE strategy is in place and operational.
- Marketing and outreach plan is in place and operational.
- Internal systems development is complete, and program has been fully integrated into PDC operating departments.

COMMUNITY AND PUBLIC BENEFIT

The CPACE Program is well positioned to provide numerous community and public benefits. Energy retrofits of commercial buildings will reduce carbon emissions and support the City/County climate action plan goals. The renovation of commercial buildings also stimulates the economy and provides business opportunities for local DBE firms, their workforce, and others in the supply chain.

PUBLIC PARTICIPATION AND FEEDBACK

PDC held a series of roundtables engaging private firms and nonprofits in the local energy efficiency industry and members from the minority contracting community to inform both program design and the certified firm support strategy. Input received with regard to the program design re-affirmed the need for this financing tool in the marketplace to facilitate a larger number and deeper retrofit of buildings. Industry members cautioned that for the program to be successful it needs to have a simple process with an ability to scale for larger projects. The minority contracting community encouraged PDC and the County to set goals for contractor certification and participation, create a program that is transparent and easy to utilize for contractors, and identify resources to support capacity building.

BUDGET AND FINANCIAL INFORMATION

PDC will allocate up to $3,000,000 from the CPRL budgets in multiple URAs to fund CPACE loans during the pilot, including Central Eastside, Downtown Waterfront, Gateway Regional Center, Interstate Corridor, Lents Town Center, and the River District. Collectively, CPRL budgets in these URAs total more than $67,000,000 over the pilot period. In addition, CPACE Program transactions will be coordinated with PDC Urban Development Department staff to ensure that they support existing URA stategies.

RISK ASSESSMENT

The primary risk associated with the CPACE pilot is that borrowers default on the CPACE loans. This risk is reduced significantly by the fact that the CPACE loan will be secured by a benefit assessment lien with seniority over all other encumbrances except general property taxes. If a CPACE lien were to default, other lien holders would have an incentive to cure the default to protect their own security. If junior lien holders did cure the default, PDC could certify the delinquent lien to the property tax role for collection.

ALTERNATIVE ACTIONS

There are a number of alternative actions the PDC Board could consider, including:

1. Approve the IGA, but limit PDC's role to program administrator and not lender. This would eliminate any risk of loss due to default of a PDC-funded CPACE loan.
2. Approve the IGA and CPACE Program Guidelines, but limit the program to specific URAs. This would further target CPACE impact in certain geographical areas of the city.
3. Not approve the IGA and instruct PDC staff to work with the City to establish a citywide CPACE program and negotiate an IGA to administer the program on the City's behalf.
4. Deny the request and cease exploration of this financing structure.

ATTACHMENTS

A. FY 2015-16 URA CPRL Budgets

FY 2015-16 URA CPRL Budgets

URA	FY 15-16 Approved	FY 16-17 Projected	FY 17-18 Projected	FY 18-19 Projected	FY 19-20 Projected	Total
Central Eastside	600,500	600,500	600,500	600,500	600,500	3,002,500
Convention Center	-	-	-	-	-	-
Downtown Waterfront	3,951,000	2,001,000	2,001,000	2,001,000	1,000	9,955,000
Gateway Regional Center	1,501,000	1,501,000	1,501,000	1,501,000	1,501,000	7,505,000
Interstate	2,472,000	2,002,000	1,277,000	1,277,000	1,277,000	8,305,000
Lents	4,502,000	15,002,000	15,002,000	1,002,000	1,002,000	36,510,000
North Macadam	-	500,000	500,000	500,000	500,000	2,000,000
River District	20,452,000	12,002,000	11,002,000	3,002,000	2,002,000	48,460,000
South Park Blocks	-	-	-	-	-	-
Willamette Industries	-	-	-	-	-	-
Total	33,478,500	33,608,500	31,883,500	9,883,500	6,883,500	115,737,500