THE CITY OF SAN DIEGO

REPORT TO THE CITY COUNCIL

DATE ISSUED: July 18, 2012 REPORT NO: 12-091

ATTENTION: Natural Resources and Culture Commitee
July 25, 2012

SUBJECT: Authorization to Join CaliforniaFIRST PACE Financing Program

REFERENCE:

REQUESTED ACTION:

1. Authorize City to join CaliforniaFIRST Program.

2. Authorize California Statewide Communities Development Authority to accept applications from property owners, levy contractual assessments and perform other actions relating to Property Assessed Clean Energy (PACE) financing.

3. Direct City Staff to pursue additional PACE options and return to the NR&C as appropriate options become available.

STAFF RECOMMENDATION: Approve Requested Actions

SUMMARY: The City of San Diego's commercial buildings number in the tens of thousands with a total square footage in the hundreds of millions. Retrofitting this building stock to reduce utility supplied energy and water consumption is consistent with City Council policies and has the potential to generate tens of thousands of new jobs in the construction, clean tech, and service sectors. However, the lack of appropriate financing is widely identified as an obstacle that makes it difficult for property owners to make these investments.

Staff recommends expanding the financing options available to City property owners for the purposes of energy efficiency, renewable energy, and water conservation improvements through an assessment-backed funding vehicle referred to as " PACE" (Property Assessed Clean Energy). The CaliforniaFIRST program is designed to achieve this aim via this action and give property owners the choices that will create a competitive market where PACE-based financial products can continue to innovate and evolve.

Assembly Bill 811 became law in July 2008, authorizing the legislative body of a City to designate an area within which willing property owners could enter into contractual assessments to finance the installation of distributed renewable energy generation, as well as energy efficiency improvements, that are permanently fixed to the property owner's residential, commercial, industrial, or other real property. Such PACE financing arrangements allow

property owners to finance energy efficiency, renewable generation and water efficiency improvements through obtaining financing that would be repaid as an item on the property owner's property tax bill. PACE financing helps make these types of investments feasible for property owners by extending access to financing, reducing the cost of capital, and allowing the repayment obligation to remain attached to the parcel upon sale.

In May 2010 the Council approved a PACE program for the City of San Diego to finance residential and commercial energy upgrades. In July of that year, Federal Housing Finance Authority ("FHFA"), the federal agency that oversees Fannie Mae and Freddie Mac, issued guidance letters opposing PACE programs and effectively halted the implementation of that effort. In the interim, PACE program options that are designed to overcome the legal issues raised by the FHFA have surfaced. Among those is the CaliforniaFIRST program as amended and restarted by California Communities.

California Communities is a joint powers authority sponsored by the League of California Cities and the California State Association of Counties. The member agencies of California Communities include all 58 counties and more than 400 other local agencies throughout California, including the City of San Diego. The CaliforniaFIRST Program is their PACE program.

Because of the guidance letters opposing PACE provided by the FHFA, the CaliforniaFIRST Program will launch initially providing only financing for non-residential properties. Should the residential regulatory environment improve, the CaliforniaFIRST program may expand to include residential financings. "Non-residential" includes properties that are commercial, multi-family with 5 or more units, industrial, and agricultural.

The CaliforniaFIRST Program will allow owners of property in participating cities and counties to finance renewable energy, energy efficiency and water efficiency improvements on their property. If a property owner chooses to participate, the improvements will be financed by the issuance of bonds by California Communities. California Communities will retain and pay the bond and disclosure counsel for issued bonds. The City will not be the issuer of the bonds. California Communities will levy "contractual assessments" on the owner's property to repay the portion of the bonds issued to finance the improvements on that property. California Communities has selected Renewable Funding LLC and RBC Capital Markets to provide administration and financing for the program including charging fees to the participants. California Communities has established a platform that is designed to enable other PACE providers to offer PACE-based financing products under the CaliforniaFIRST program.

The CaliforniaFIRST Program "contractual assessment" proceedings will be undertaken by California Communities pursuant to Chapter 29 of Division 7 of the Streets & Highways Code, which was amended in 2008 by Assembly Bill 811 and further amended in 2009 by Assembly Bill 474, to allow the financing of renewable energy, energy efficiency and water efficiency improvements on private property. Pursuant to Chapter 29, assessments may be levied to finance renewable energy, energy efficiency and water efficiency improvements only with the free and willing consent of the owner of each lot or parcel on which an assessment is levied at the time the assessment is levied. Property owners must evidence their consent to the assessments by

executing a contract with California Communities. Since the contractual assessment will have priority over pre-existing private liens, such as mortgages, notice to, and particularly with non-residential properties, written notification/consent/acknowledgement from all mortgage holders of the property will be required as a condition of participation. Within the City of San Diego the California Communities would utilize an existing county-wide AB 811 district established March 10, 2010.

The benefits to the property owner include:

- Only property owners who choose to participate in the program will have assessments imposed on their property.
- Increased access, lower cost and longer payback terms for capital to finance energy/energy efficiency/water efficiency investments.
- Potentially lower ongoing operating costs resulting from more efficient energy and water usage, and increased property values associated.
- Potentially increased property values associated with properties and facilities that use energy and/or water resources more efficiently and/or generate clean energy.
- Under the CaliforniaFIRST Program, the assessment obligation will transfer with the property upon sale. This is preferable to non-PACE loans which are due on sale of the benefited property, making it difficult for property owners to match the life of the repayment obligation with the useful life of the financed improvements.
- The property owner can choose to pay off the assessments at any time, subject to applicable prepayment penalties.
- Regional aggregation and standardization provided by the CaliforniaFIRST Program is designed to provide the program scale and the investment sizing to attract private capital providers.

The expected benefits to the City include:

- As in conventional assessment financing, the City is not obligated to repay the bonds issued by California Communities or to pay the assessments levied on the participating properties.
- California Communities is responsible for and handles all assessment administration, bond issuance and bond administration functions while requiring virtually no City staff time to administer the program. At the same time, the program gives the City the option to employ City resources such as enhanced marketing and outreach as later determined by the City.

The proposed resolution authorizes California Communities to accept applications from owners of property within the City of San Diego for municipal financing of renewable energy, energy efficiency and water efficiency improvements through the CaliforniaFIRST Program. It also authorizes California Communities to conduct assessment proceedings and levy assessments against the property of participating owners within our boundaries. It also authorizes miscellaneous related actions and makes certain findings and determinations required by law. California Communities has undertaken a judicial validation proceeding as part of its initiation of the CaliforniaFIRST Program which included noticing in San Diego County. The proceeding protest period closed June 11, 2012 without challenge. The judge's ruling finalizing the validation is anticipated by late July. Upon successful completion of this validation as

determined by the City Attorney, the CaliforniaFIRST Program would commence with the placing of assessments on participating properties.

Any jurisdiction can withdraw from the CaliforniaFIRST Program at any time by passing a resolution rescinding the authorization. Participating jurisdictions are also free to develop and operate other financing programs, including alternative PACE programs, independently of but concurrent to CaliforniaFIRST.

In addition to joining CaliforniaFIRST, staff recommends that additional PACE financing options continue to be pursued. In the near term there are at least two additional PACE avenues that the City could consider pursuing. The first is to make programs available that utilize an SB 555 district. SB555 is a PACE-enabling law that was passed subsequent to AB 811. SB 555 PACE programs could potentially expand the scope of PACE financing to areas not covered by AB811. The second is joining CalPACE, a program run by the California Economic Development Authority JPA. The program backers plan to seek a judicial validation for this program which could be completed by November 2012.

FISCAL CONSIDERATIONS:
The action before the committee does not have a fiscal impact.

PREVIOUS COUNCIL and/or COMMITTEE ACTION:
Council adopted R-2012-164, retention of outside counsel to form an assessment program/district under Assembly Bill 811 (AB 811) and provide related services on December 6, 2011,
Council adopted R-2011-145, establishing policy goals for home energy retrofit retrofit programs in the City of San Diego on September 13, 2010.
Council adopted R-2010-751, establishing City of San Diego Renewable Energy, Efficiency and Water Conservation Improvement District No. 1 on May 11, 2010.
Council adopted R-2010-754, approving the administration agreement for the Clean Generation Program on May 4, 2010.
Council adopted R-2010-752, determining the necessity to incur bonded indebtedness for City of San Diego Renewable Energy, Energy Efficiency and Water Conservation Improvement District No. 1 on April 27, 2010.
Council adopted O-2010-98, levying special taxes within City of San Diego Renewable Energy, Energy Efficiency and Water Conservation Improvement District No. 1 on April 27, 2010,
Council adopted R-2010-650, authorizing the Intention to Incur Indebtedness with respect to the City of San Diego Renewable Energy, Energy Efficiency and Water Conservation Improvement District No. 1 on March 24, 2010.
Council adopted R-2010-640, authorizing the Intention to Establish the City of San Diego Renewable Energy, Energy Efficiency and Water Conservation Improvement District No. 1 on March 24, 2010.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS:
Community, stakeholder and public outreach has been ongoing since November 2010 in the formulation and development of PACE policy. Environmental Services and Mayor's Office staff

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Community, stakeholder and public outreach has been ongoing since November 2010 in the formulation and development of PACE policy. Environmental Services and Mayor's Office staff have engaged from property owners, contractors, financiers, lenders, community groups, energy non-profits and industry groups.

California Center for Sustainable Energy, February 1, 2011
Sustainable Energy Advisory Board, February 8, 2011
California Center for Sustainable Energy, February 22, 2012
California Center for Sustainable Energy, March 9, 2012
Energy Efficiency Roundtable, March 13, 2012
SANDAG Energy Working Group March 22, 2012
Sunshot Financing Working Group, April 11, 2012

KEY STAKEHOLDERS AND PROJECTED IMPACTS:
Eric Engelman
Originating Department
Julie Dubick
Chief of Staff

Eric Engelman
Originating Department

Julie Dubick
Deputy Chief/Chief Operating Officer