



THE CITY OF SAN DIEGO
REPORT TO THE CITY COUNCIL

DATE ISSUED: March 20, 2014 REPORT NO: 14-031
ATTENTION: Council President and Members of the City Council
SUBJECT: Proposed City Participation in the Home Energy Renovation Opportunity (HERO) and FigTREE Residential Property Assessed Clean Energy (PACE) Programs
REFERENCE: The Environment Committee, Committee of the City Council of the City of San Diego- February 5, 2014

REQUESTED ACTIONS:

1. Approve a resolution to allow Western Riverside Coalition of Governments (WRCOG), as the administrator of the Home Energy Renovation Opportunity (HERO) PACE Program, to offer the program to owners of residential property in the City of San Diego under the conditions outlined in this report
2. Approve a resolution to allow the California Enterprise Development Authority, as the administrator of the Figtree PACE program, to offer the program to all owners of residential property in the City of San Diego under the conditions outlined in this report

STAFF RECOMMENDATIONS: Approve the Requested Actions

SUMMARY:

At the Environment Committee on February 5, 2014, staff was directed to:

1. Prepare all necessary Council authorizations to allow the City to participate in the California HERO program as administered by the Western Riverside Council of Governments (WRCOG) joint powers authority.
2. Prepare a resolution to allow the California Enterprise Development Authority, as the administrator of the Figtree PACE program, to offer the program to the owners of all residential property in the City.
3. Prepare all necessary Council authorizations for the City to enter into an agreement with Ygrene Energy Fund to form and administer a special tax district pursuant to the Mello Roos Act, as amended by SB 555.

This action is asking approval for the first two items. The third item will be brought back to City Council as a separate action.

BACKGROUND:

Property Assessed Clean Energy or “PACE” programs allow property owners to finance energy efficiency, water conservation, and renewable energy projects on existing residential and commercial structures through a special tax or assessment on the property. PACE financing programs can be set up and administered under either of two different statutory frameworks:

1. The Improvement Act of 1911 (Improvement Act) as amended by AB 811 or
2. The Mello-Roos Act as amended by SB 555.

While both SB 555 and AB 811 PACE programs accomplish the same purpose, several important statutory and structural differences exist between programs that operate under these statutes. There are also differences in the level of City administrative involvement required between the two types of programs. Under AB 811, programs are turnkey requiring minimal City staff time, while SB 555 programs require additional City resources to set up as well as ongoing City administrative oversight.

1. The Improvement Act of 1911, as amended by AB 811, allows for the formation of assessment districts to provide for the financing of clean energy improvements on private property. Under AB 811:
 - a. Property owners enter into a contractual assessment to finance the cost of energy efficiency, renewable energy and water efficiency improvements to their property. Funds are loaned to the property owner to pay for the improvements.
 - b. The loan is secured by a lien on the property and is repaid by an assessment. The assessment is paid at the same time and in the same manner as other property taxes. Assessment liens are superior to most other existing liens on the property, including mortgages.
 - c. There is generally little to no cost or administrative burden for cities where the assessment district is formed by a joint powers authority (“JPA”) Joining or associating with a JPA also reduces the legal exposure of the city.

Both Figtree and HERO programs are assessment districts formed pursuant to AB 811. Figtree was approved by the City Council for commercial properties and for residential properties with no mortgage liens in October 2012. The HERO program is not currently authorized to operate in the City.

2. The Mello-Roos Act of 1982, as amended by SB 555, authorizes the formation of Community Facilities Districts (“CFDs”) to finance the acquisition, installation and improvement of energy efficiency, water conservation and renewable energy systems on real property.

HERO Program (AB 811)

The Western Riverside Council of Governments (WRCOG) launched a residential PACE program in January 2012 known as the "Home Energy Renovation Opportunity" (HERO) program.

WRCOG is a Joint Powers Authority (JPA) with 18 member jurisdictions in western Riverside County. HERO is operated by the San Diego based company, Renovate America.

As with all AB 811 programs the California HERO program uses “land-secured” financing, wherein a contractual assessment lien is placed on the property to secure a loan, the proceeds of which are used to pay for the installation of authorized improvements on the property. The loan is repaid over a 5 to 20 year term, depending on the expected useful life of the improvements financed. The assessments also pay for the costs of issuing bonds and administering the program. The contractual assessment installments are collected on the county property tax bill. If the owner sells the property, the contractual assessment obligation may remain an obligation of the property.

Additionally, because FHFA has instructed Fannie Mae and Freddie Mac not to purchase loans with PACE assessments such as those offered by the HERO program, property owners who sell or refinance their property may be required to prepay such assessments at the time they close sale or refinancing. Also, under the California HERO program, if a property owner fails to pay the annual contractual assessment installments, the Authority is obligated to remove the delinquent installments from the property tax bill and commence foreclosure proceedings to collect the delinquent installments.

Several San Diego jurisdictions including the cities of Carlsbad, San Marco, Vista, Lemon Grove, Oceanside, and Solana Beach have recently adopted the HERO program. There are 76 jurisdictions in the State of California that have approved resolutions to participate in HERO.

The HERO program is available in 14 counties statewide, has created over 1,300 new jobs and generated more than \$443,000,000 in economic stimulus for the State.

FigTree PACE (AB 811, formerly California PACE)

FigTree is a San Diego-based clean energy finance company providing PACE financing for energy efficiency, renewable energy and water conservation upgrades. FigTree’s PACE program allows owners to finance improvements and pay for them over a defined period of time through an assessment collected on their property tax bill. FigTree recently completed its judicial validation so that it can now begin financing PACE projects in the City of San Diego. The minimum amount required to be financed is \$5,000. Interest rates range from 6-8% and the maximum term is 20 years but cannot exceed the useful life of the improvements. Lender consent is required.

On October 23, 2012, the City Council authorized the City to join a “Commercial PACE” program called “California PACE” (now known as Figtree). The California Enterprise Development Authority (CEDA) was authorized to accept applications from eligible commercial property owners including multi-family properties, and single family residential property with no mortgage liens.

On June 7, 2013, the City entered into an agreement with Figtree and CEDA to establish and administer a PACE program within the boundaries of the City of San Diego. Currently, the Figtree PACE program is limited to commercial properties and to residential properties with no mortgage lien attached.

On February 5, 2014, the City's Environment Committee authorized staff to prepare a resolution to allow CEDA, as the administrator of the Figtree PACE program, to offer the program to all owners of residential property in the City

DISCUSSION:

At the October 10, 2012 NR&C meeting, the Committee requested a legal analysis of the HERO residential PACE program. Subsequently, both the City Attorney's Office and the Debt Management Department Staff were asked to review the HERO residential PACE program. In these reports there were some concerns identified regarding the implications and outstanding issues with FHFA restrictions on mortgages encumbered by PACE liens and the potential negative impact to homeowners.

City Attorney's Legal Analysis

Per the City Attorney's analysis, the proposed HERO program's legal structure and associated lien priority issues raised by FHFA have not been resolved and present potential risks to homeowners who participate in the program. More details are provided in the attached memo (Attachment 1) from the City Attorney's office.

Debt Management Department's Review

Per Debt Management's review, if the City authorizes participation in the HERO program, program provider disclosures and any City links to the HERO program (and all other City authorized PACE programs) should advise property owners they may wish to consider all PACE and non-PACE financing vehicles that may be available to them to ensure the best financing terms possible for the property owners' individual situations. Also, the program literature made available to residential property owners should describe the potential risks due to the FHFA restrictions such as reduced ability to refinance, potential default of the mortgage, reduced ability to sell the property, and mandatory early lien pay-off. The purpose of disclosing this information is to ensure the property owner can weigh these issues carefully to make an informed decision.

PACE Loss Reserve Program

In September, 2013 Governor Brown signed SB 96, authorizing the establishment of the "PACE Loss Reserve Program" to address FHFA's concerns. Under SB 96, the Loss Reserve would be used to make mortgage lenders whole for any direct losses incurred due to the existence of a PACE lien on a property during a foreclosure or forced sale. FHFA has not taken any action to acknowledge or loosen their stance regarding PACE since passage of SB 96. The guidelines for the PACE Loss Program are included in Attachment 2.

Conclusions and recommendations

Although FHFA concerns remain, given the establishment of the PACE Loss Reserve Program as well as the success of the PACE programs such as HERO, staff recommends that the City of San Diego move forward with the proposed options for establishing a residential PACE Program for City residents. It is further recommended that the following underwriting criteria are required for Program Participation:

1. The applicant(s) must be the property owner(s) of record. If the legal property owner is a corporation, trust or similar legal entity, the applicant must be authorized to act on behalf of such entity.
2. Property owner(s) must be current on all property taxes for the property; No late payment levied on the property more than once during the prior three years or since the purchase of the property.
3. Property owner(s) must be current on their property debt for the prior twenty four (24) months;
4. Property owner(s) have not declared bankruptcy in the past seven (7) years and the property is not currently an asset in a bankruptcy proceeding;
5. Total existing secured indebtedness (including mortgage and other special tax and assessment liens) in combination with the PACE lien, does not exceed 95% of the existing property value.
6. Property must not have any involuntary liens, including construction liens.

FISCAL CONSIDERATIONS:

Some minimal staff time, to be absorbed by existing staff, will be required for all work related to joining and monitoring the two programs the City Council is being asked to authorize. All costs related to energy efficiency, water conservation, and/or renewable energy projects will be borne by the property owner.

PREVIOUS COUNCIL AND/OR COMMITTEE ACTION:

- Environment Committee – February 5, 2014
 - Staff authorized to prepare all necessary Council authorizations to allow the City to participate in the California HERO program as administered by the Western Riverside Council of Governments (WRCOG) joint powers authority;
 - Staff authorized to prepare a resolution to allow the California Enterprise Development Authority, as the administrator of the Figtree PACE program, to offer the program to the owners of all residential property in the City.
 - Staff authorized to prepare all necessary Council authorizations for the City to enter into an agreement with Ygrene Energy Fund to form and administer a special tax district pursuant to the Mello Roos Act, as amended by SB 555.
- City Council Meeting – October 23, 2012
 - Council adopted R-307792, retention of outside council (Stradling, Yocca, Carlson & Rauth) in connection with the City's SB555 PACE program, not to exceed \$130,000, for such legal services.
 - Council adopted R-307793, authorizing execution of Associate Membership Agreement for membership in the California Enterprise Development Authority.
 - Council adopted R-307794, authorizing participation in the FigTree PACE program; authorizing the California Enterprise Development Authority to accept applications from eligible property owners, conduct contractual assessment proceedings and levy contractual assessments within the territory of the City of San Diego.
- The Committee on Natural Resources and Culture – October 10, 2012:
 - City Attorney's Office was directed to proceed with legal analysis for joining the HERO residential PACE program. Upon completion of the legal analysis, staff would

- report back to NR&C with the actions necessary to opt into the HERO residential PACE program.
- Staff was authorized to work with the City Attorney's Office to draft the documents and proceed to City Council with the necessary actions to opt-in to the FigTree Commercial PACE (formerly California PACE) program
 - City Attorney's Office was directed to proceed with Council Action seeking approval to retain outside legal counsel for analysis and preparation of documents to form an SB555 district. Upon completion of the legal analysis and document preparation, staff would report back to NR&C with the actions necessary to establish an SB555 program.
 - City Council Meeting – September 18, 2012:
 - Council adopted R-2013-117, opting into CaliforniaFIRST PACE financing program and reaffirming direction to develop additional PACE options.
 - The Committee on Natural Resources and Culture (NR&C) – July 25, 2012
 - Approved action entering City into CaliforniaFIRST PACE financing program and directed staff to develop additional PACE financing options.
 - Directed staff to hold an informational stakeholder meeting, and return October 10, 2012 with report on California PACE and SB555 options as well as proposed program performance metrics and present to NR&C in one year on those metrics.
 - City Council Meeting – December 6, 2011
 - Adopted R-2012-164, retention of outside counsel to form an assessment program/district under Assembly Bill 811 (AB811) and provide related services.

COMMUNITY PARTICIPATION AND OUTREACH EFFORTS:

From November 2010 through September 2012 interested property owners, contractors, lenders, community groups, energy non-profits and industry groups were engaged in stakeholder and community outreach efforts.

KEY STAKEHOLDERS AND PROJECTED IMPACTS:

While PACE providers will derive direct financial benefit from program adoption, successful program implementation will also provide significant benefit to the City of San Diego through clean energy, energy efficiency, and water conservation improvements, jobs creation, and reductions in greenhouse gas emissions.



Chris Gonaver
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Tony Heinrichs
Deputy Chief Operating Officer

Attachment 1: Office of the City Attorney Memorandum of June 5, 2013

Attachment 2: PACE Loss Reserve Program – Regulations