Identifying Opportunities for Financing Multi-tenant Projects

Energy Efficiency Finance Forum: May 2013

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According to an estimate by the U.S. Department of Energy, 30% of energy in buildings is used inefficiently or unnecessarily and every year $20 billion can be saved if the energy efficiency of commercial and industrial buildings improved by 10 percent. – (DOE 2012)
Overview Of The Market

- Scaling EE retrofits is a $279 billion investment opportunity.
- Create > 3.3 million new direct and indirect cumulative job years in the U.S.
- Mitigate over 600 million metric tons of CO₂ per year (~10% of US emissions in 2010).
- Biggest opportunity in residential space. – (Deutsche Bank & The Rockefeller Foundation 2012)

Energy use (quadrillion BTU)

- Industrial
- Commercial
- Residential
- Transportation

Expected growth from 2011-2040:
- Transportation .7%
- Residential 6.7%
- Commercial 17.3%
- Industrial 18.2%

(EIA 2013)


Common Energy Efficiency Barriers

Split-incentives with multi-tenant buildings
- Neither the owner nor tenant wants to bear the cost of the retrofit because the other will gain
- Long lease lengths make it difficult to negotiate retrofits because parties prefer letting leases expire to amending existing leases

Valuation
- Customers do not see the value in spending money to install EE upgrades
- Banks rarely consider energy efficiency investments when underwriting

Competing investment priorities
- Buildings are required or urged by various entities to install systems, making environmental upgrades potentially a lower priority

Upfront capital costs
- Limited debt capacity for Class B and C buildings
- Long payback periods
Owner-Tenant Models And Challenges

- Buildings are owned and managed in a variety of ways
- Different markets have very different needs and opportunities
- No one size fits all approach to attractive financing

**Single-tenant buildings are easier to reach**

**Owner-occupied**
- Challenges – good credit and proof that savings outweigh costs

**REIT**
- Challenges - proof of increased building value

**Multi-tenant and multi-family buildings are harder to reach**

**Owner Pays**
- Challenges – tenant space is invaded, leases must be renegotiated.

**Tenant Pays**
- Challenges – payback period of upgrades, owner’s approval to renovate space, support of other tenants.
# Financing Mechanisms

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<th>Mechanism</th>
<th>Upsides</th>
<th>Downsides</th>
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<td>On-bill financing/On-bill repayment</td>
<td>Can be structured to “follow the meter,” decreasing upfront capital cost and stretching repayment out over a long period.</td>
<td>Availability is still limited and there is not much capital available for large projects. Best for small businesses.</td>
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<td>Property assessed financing (PACE)</td>
<td>No upfront cost, ability to transfer ownership, financing is off balance sheet.</td>
<td>Needs significant regulatory support and standardization at the state level.</td>
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<td>ESCO financing</td>
<td>Provides turnkey project development. ESCOs assume technical and performance risks of projects.</td>
<td>MUSH markets are preferred because those buildings typically have stable energy loads and good credit.</td>
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<td>Energy service agreement (ESA)/Managed energy service agreements (MESA)</td>
<td>Mitigates high upfront capital costs and does not require enabling legislation. The investment fund pays for and installs the upgrades.</td>
<td>This relatively new structure. Potential legal ramifications of changes to FASB.</td>
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<td>Performance-based contracting</td>
<td>No upfront capital costs. Repayment is calculated through savings.</td>
<td>Buildings with good credit are preferred for these projects.</td>
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## Complimentary Solutions

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<td>Credit enhancement financing mechanisms reduce the risk to the financer and can extend the payback period</td>
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<td>Green leases reduce the split-incentive problem</td>
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<td>Sub-metering can assist tenants in controlling their energy use and potentially drive demand for improvements</td>
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<td>Comprehensive benchmarking, which includes recording, reporting and utilizing data appropriately, can help green leasing and financers make sound investment decisions</td>
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New York City Case Study

- High potential for efficiency in Class B and C buildings.
- Greener, Greater Buildings Plan:
  - Large buildings must benchmark efficiency annually
  - Conduct an audit and retro-commissioning study every 10 years
  - Upgrade lighting to meet code and install sub-metering
  - Adopt the local energy code – (PlaNYC 2012)

The city estimates that the laws will generate $700 million in savings and create roughly 17,800 construction jobs over ten years – (IMT 2012)


Seattle Case Study

Seattle LEED or Energy Star Certified Market (sq. ft.)

- Class A: 22,024,017
- Class B: 71,235,624
- Class C: 45,479,729

(Costar 2012)

In January 2010, the Seattle City Council passed CB 116731, establishing mandatory energy performance disclosure in commercial and large multi-family buildings. – (BetterBricks and Cushman & Wakefield)

- Seattle’s hydropower base makes energy significantly less expensive than in other parts of the U.S.
- Many Class C buildings are targeted for demolition and redevelopment.
- Puget Sound Energy works with designers and developers of major remodels and new commercial facilities, and proposes cost-effective energy efficient upgrades that exceed energy codes or standard practice – (PSE 2011)

Questions?

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