



# City of Sunnyvale

## Agenda Item

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**16-0585****Agenda Date: 5/15/2017**

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### **REPORT TO SUSTAINABILITY COMMISSION**

#### **SUBJECT**

Adopt Resolutions Authorizing the Operation of Property Assessed Clean Energy (PACE) Financing Programs Within the City of Sunnyvale, Authorize the City Manager to Execute Agreements and Other Documents Necessary to Implement the Same, and Find that the Actions are Exempt from Environmental Review under CEQA Guidelines Section 15378(b)(4)

#### **REPORT IN BRIEF**

Property Assessed Clean Energy (PACE) financing programs are an emerging lending mechanism that property owners can use to finance certain home improvement investments such as energy or water efficiency, renewable energy, or seismic retrofits. In California, PACE programs are enabled through two different laws, AB 811 and SB 555, with additional laws clarifying and expanding program parameters. Authorization by the City Council is necessary for the programs to conduct business in the City, per the requirements of AB 811 and SB 555. Encouraging installations of energy efficiency improvements through PACE financing is a component of the City's Climate Action Plan.

Several PACE providers have expressed an interest in offering their programs in Sunnyvale. In order to bring additional PACE programs to Sunnyvale, the City Council must adopt a resolution to sponsor the program and join the associated Joint Powers Authority.

Staff has evaluated the PACE program market, reviewed various program and JPA documents, and coordinated with neighboring communities, which are also reviewing opportunities to sponsor additional PACE programs. Additionally, staff has reviewed recent efforts by the Association of Bay Area Governments (ABAG) to facilitate a more level playing field among PACE programs and ensure key consumer protections are in place and that local governments have access to local program performance data. These critical terms and conditions form the basis of ABAG's Regional Collaborative Services Agreement.

PACE Program assessments are a new financial mechanism that can also present potential risk to the property owner. Staff is proposing that Sunnyvale establish additional operating conditions for PACE providers aimed at ensuring that property owners are made aware of these potential risks and understand the implications that entering a PACE assessment can have on their current mortgages and future property transactions.

#### **BACKGROUND**

Energy efficiency retrofits of existing building stock are an essential strategy to reducing greenhouse gas emissions. While new buildings and homes are subject to increasing efficiency standards, many communities including Sunnyvale, have a large inventory of older buildings and homes that are inefficient. These buildings can be less comfortable and more costly to heat or cool. Retrofitting existing buildings and homes through projects such as new insulation or replacing aging heating and

cooling systems can be a sizeable investment even with available rebates and incentives.

PACE financing is a funding mechanism designed to assist property owners with energy efficiency, renewable energy, and water conservation projects. PACE programs provide financing without a down payment or up-front capital costs. PACE financing is available to residential, commercial, and industrial properties, covers the project's full cost, and can be repaid over long periods of up to 20 years as an additional assessment on the property that is paid with the property tax bill.

PACE financing is growing in popularity with more than \$1.5 billion in projects financed in California to date, primarily for single family homes. Additional providers have entered the marketplace as PACE growth continues. Currently, the City of Sunnyvale has one active PACE program (CaliforniaFIRST). In recent months Sunnyvale, along with many South Bay communities, has been approached by additional PACE providers seeking to expand their service territory.

## **EXISTING POLICY**

### **Climate Action Plan (CAP)**

*Decrease Energy Consumption (EC)* - Goal to improve energy efficiency and conservation in the community and City operations.

- EC-3.1 Participate in a PACE or similar financing program to offer low-interest loans to residents for energy-efficiency upgrades.
- EC-4.2 Participate in a PACE or similar financing program to offer low-interest loans to businesses for energy efficiency upgrades.

*Provide a Sustainable Energy Portfolio (EP)* - Goal to increase the amount of renewable energy produced in the city and facilitate a higher renewable mix for energy delivered to the city.

- EP-2.2 Participate in a PACE or similar financing program to offer low-interest loans to residents and businesses for renewable energy installations.

### **General Plan, Chapter 5: Housing**

- Goal HE-6 Sustainable Neighborhoods and Community Vision Sunnyvale has adopted a sustainability policy to become "a regional leader in environmental sustainability, advocating to reduce dependence on non-renewable resources by providing greater transportation options, reducing waste, protecting our natural resources, and promoting alternative energy usage and research."

## **ENVIRONMENTAL REVIEW**

The action being considered does not constitute a "project" within the meaning of the California Environmental Quality Act ("CEQA") pursuant to CEQA Guidelines section 15378(b)(4) in that it involves a government fiscal activity or funding mechanism that does not involve any commitment to a specific project that may result in a potentially significant physical impact on the environment. If individual projects funded by PACE loans require discretionary approvals from the City, the environmental impact of those projects will be evaluated at the time of approval. Rooftop solar projects are statutorily exempt from CEQA under Public Resource Code Section 21080.35.

## **DISCUSSION**

### **PACE Financing Mechanism**

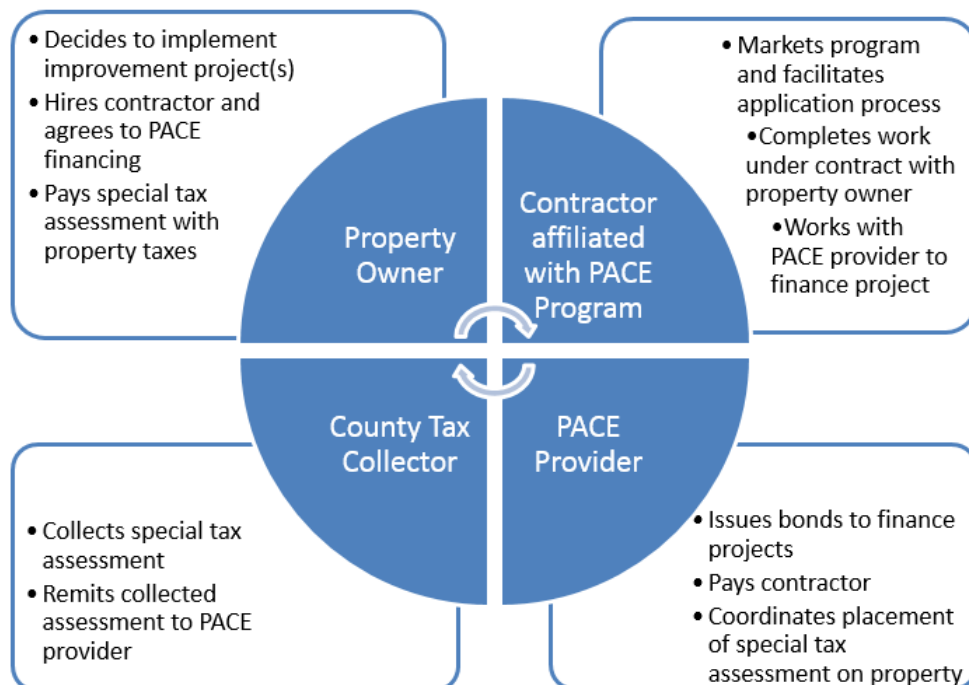
PACE programs can be set up and administered under either of two statutory frameworks: the

Improvement Act of 1911 as amended by AB 811 (2008) and the Mello-Roos Act as amended by SB 555 (2011). Under AB 811 programs, the property owner voluntarily enters a contractual assessment agreement to join a special tax district. The loans are secured by a lien recorded on the property. Under SB 555 programs, the property owner “votes” to annex his or her property into a specially-created community facilities district (CFD). The loans are repaid via special tax assessments. Under both types of programs, the owner’s loan payments are collected along with property taxes.

Although cities can directly administer their own PACE programs under either AB 811 or SB 555, most PACE programs operate under a joint powers authority (JPA) structure. JPAs are public entities created by an association of other public entities such as cities and counties. The JPA usually contracts with a private PACE provider to administer the program. The JPAs issue bonds to fund the loan program or may obtain funds through private equity investment.

The PACE provider arranges capital, administers programs, partners with local contractors, and places special tax assessments in coordination with county tax collectors. PACE financing programs are primarily marketed through contractors that are affiliated with specific PACE providers. Property owners hire a participating contractor, implement qualified home upgrades, and pay back the PACE loan through property tax bills.

Once a city acts to sponsor a PACE program, the City has no direct role in PACE program implementation or in the assessment transactions. The figure below generally depicts how PACE programs operate.



PACE loans are distinct from other financing options (e.g., home equity loans) because the PACE loans are:

- approved based on equity of the property, not personal credit history;
- recorded as a special assessment or lien on the property's tax bill;
- stay with the property and are generally transferrable upon its sale; and
- "senior" to other debts and must be repaid before mortgage debt.

These conditions can be attractive to property owners who may not have access to other lines of credit or may not be planning to keep the property long-term. However, these conditions can also present risks to program participants. These defining conditions, including the fact that the PACE assessment can take a "senior" position to existing mortgages, present a challenge for homeowners who wish to refinance or sell their homes. The Federal Housing and Finance Administration issued a statement in July 2010 advising that PACE programs "pose unusual and difficult risk management challenges for lenders, servicers, mortgage security investors" which resulted in Fannie Mae and Freddie Mac specifying that they would not purchase mortgages with senior priority PACE liens.

To address the FHFA's concerns, in September of 2013, Governor Jerry Brown signed Senate Bill 96 into law, which established a PACE Loss Reserve Program. This reserve would cover any losses incurred by a first mortgage lender resulting from a PACE assessment being paid before the outstanding balance due to a forced sale. This action was intended to address the FHFA concern; however, the FHFA has not changed its position. To date, the reserve has not been accessed. Recently, Fannie Mae introduced an alternative program called HomeStyle Energy which allows borrowers to finance clean energy upgrades equal to up to 15 percent of the appraised value of their home. HomeStyle Energy loans can also be used to pay off existing PACE loans.

The senior position of PACE loans also creates a potential risk to the property owner in other ways: (1) the property owner could be considered in default of their existing mortgage if they did not get lender consent prior to agreeing to the PACE assessment; or (2) the property owner may be required to pay off their PACE loan at the time of resale or refinance. Adequate disclosures to potential applicants helps to ensure that property owners are made aware and considering these risks as they agree to the PACE assessment. Additionally, some PACE providers have established policies that may facilitate a contractual subordination of the PACE assessment to the mortgage, if so requested by the mortgage lender.

Lenders may also require the property owner to pay off the PACE assessment at time of refinance or resale. Real estate agents may also advise their clients to pay off the PACE assessment to simplify a property sales transaction. Staff has learned that some PACE providers charge differential interest rates or penalties for early pay off of the PACE assessment, even if required by the mortgage lender.

Additionally, interest rates and fees also vary by PACE program and last year AB 2693 (PACE Preservation and Consumer Protections Act) became effective on January 1, 2017, and further establishes standardized disclosures and protections for consumers and specifically requires that all California PACE providers provide customers with a three-day right-to-cancel and a Financing Estimate and Disclosure Statement similar to other home loans.

Association of Bay Area Governments (ABAG) Regional Services Collaborative Agreement (Regional

Agreement)

As the issuance of bonds and oversight of financial functions is controlled by the JPAs and outreach is conducted by the program contractors, local jurisdictions have had limited control over local PACE activities. Participating communities have had challenges obtaining activity reports from some PACE providers and have expressed concerns about consumer protections. Many PACE providers operate under their own set of consumer protection policies with differing terms.

To support best management practices for PACE throughout the Bay Area region, the Association of Bay Area Governments (ABAG), through BayREN, has recently developed a Regional Collaborative Services Agreement (Regional Agreement). PACE providers that sign on to the ABAG Regional Agreement are committing to operating under a common set of established terms and conditions.

The ABAG Regional Agreement addresses key areas of concern for local governments including:

- monitoring PACE provider activities in regards to consumer protections practices;
- improving program reporting and transparency to local governments; and
- co-marketing of energy efficiency programs offered by the city or county (e.g., financing programs offered by City of Sunnyvale's Housing Division).

The ABAG Regional Agreement assures ABAG member jurisdictions who sign onto the agreement that its terms and conditions will apply to PACE providers that have signed on to the ABAG Regional Agreement and are authorized to work in their community. To date, the following five PACE providers have signed the ABAG Regional Agreement: HERO; PACE Funding Group; Ygrene; Figtree; and AllianceNRG.

Staff believes that the ABAG Regional Agreement provides value to local communities and addresses some challenges that local communities working with PACE providers have experienced. It sets requirements for certain financial disclosures and provides a standard set of expectations for how PACE providers interact with local communities and participating property owners. It ensures that local communities receive timely information and data from PACE providers including participation rates, types of projects financed, and energy and water savings. Additionally, it provides a mechanism whereby PACE providers collaborate with local communities to provide information on other energy programs.

PACE Programs interested in Operating in Sunnyvale

PACE programs that have expressed interest in operating in Sunnyvale include:

- California Home Energy Renovation Opportunity (HERO) by Renovate America
- Ygrene Energy Fund California LLC (Ygrene)
- Figtree Company, Inc. (Figtree)
- Open Pace which includes multiple providers including PACE Funding Group

To make additional PACE programs available in Sunnyvale, the City must pass separate resolutions to sponsor individual programs and join a specific JPA partnered with each PACE provider. The California Statewide Community Development Authority recently created the OpenPACE platform, which provides a city with access to multiple pre-qualified PACE providers by adopting a single resolution. Providers participating in OpenPACE are: CaliforniaFIRST, PACE Funding Group,

AllianceNRG, CleanFund, and Spruce.

A detailed comparison of the abovementioned programs is provided in Attachment 2 that includes information on program reach, performance history, interest rates, and loan terms for the different operating PACE programs.

#### Benefits of Expanding the PACE Program Market in Sunnyvale

The existing City grant and loan programs for energy efficiency are only available to lower-income home owners, while the Bay Area Home Energy Upgrade program covers only larger upgrades and does not cover renewable energy projects. Opening the local market to additional PACE providers creates a diversity of financing options for Sunnyvale residents and businesses interested in making energy efficiency, water efficiency, or renewable energy upgrades.

PACE financing promotes projects that help to lower the community's overall greenhouse gas (GHG) emissions in keeping with the City's CAP. PACE or similar financing programs are identified in four CAP actions to advance residential and commercial energy efficiency and local residential and commercial renewable energy adoption. The CAP Work Plan identified that staff would monitor participation in CaliforniaFIRST and would evaluate if additional outreach and/or PACE program providers are needed.

CaliforniaFIRST has been the sole PACE program available in Sunnyvale since August 2014. The City Council adopted a resolution to authorizing the City to participate in the formation of CaliforniaFIRST in January 2010. Since 2014, this program has provided 8 residential loans for a total value of \$204,188 in the City. All of the projects were renewable energy projects. This modest participation rate, coupled with the recent interest from contractors and PACE providers to work in Sunnyvale, provides a basis for expanding program access. PACE providers operate and support non-exclusive market conditions and many local jurisdictions have sponsored multiple PACE programs.

#### Conclusion

As discussed above, there are risks associated with PACE financing and there have been reports of home owners in California, generally in economically depressed areas of the state, who experienced challenges with refinancing or selling their property due to a PACE assessment. In the Bay Area, where housing values and demand are high, most buyers pay off the PACE lien in order to qualify for a conventional mortgage. Fannie Mae's HomeStyle Energy Program now provides another option for homeowners to pay off PACE liens if needed to sell or refinance their property. In addition, although Fannie Mae and Freddie Mac have not changed their position, in 2016 the FHA began insuring mortgages with PACE liens as long as the lien does not have first priority, cannot accelerate (i.e. the entire amount cannot become immediately due and payable as a result of missed payments) and there are no limitations on transfer of the lien to a new homeowner

PACE financing is a valid mechanism for financing energy and water efficiency projects. As with most financial products, property owners must exercise due diligence to ensure they are fully aware of the financial implications and risks. After review of the prospective providers' customer documents and meeting with each provider, staff is recommending that the City establish additional operating conditions for PACE Providers in order to operate in Sunnyvale, these include:

- Provider has signed and agrees to implement the ABAG Regional Agreement;

- Provider agrees to offer contractual subordination of the PACE assessment upon property owner or mortgage lender request;
- Provider has demonstrated to staff that disclosures of risk to existing mortgages and FHFA's position are provided to property owners at the time of application and agrees to continue to provide this information at the application stage; and
- Provider will not charge differential interest rates or pre-payment penalties for early payoff of the PACE assessment.

While these additional requirements do not completely mitigate all potential risk, staff believes that these conditions are in the best interest of our community and will help to better ensure that property owners are provided with information about terms, conditions, and risks prior to agreeing into a PACE assessment. The conditions would be included in a Letter of Agreement (Attachment 3) to be signed by the PACE providers in order for the City to sponsor the program.

Staff has presented these proposed conditions to the PACE providers and the following have indicated that they are able and willing to sign the City's proposed Letter of Agreement: HERO, Open PACE, Ygrene, FigTree.

Open PACE has reviewed the letter and has indicated that the providers that are a part of the Open PACE program that have also signed the ABAG Agreement will be willing to sign. Staff is recommending that the City "Opt-In" to the Open PACE program and only authorize only those providers that have signed the Letter of Agreement and the ABAG Agreement (at this time this would include Pace Funding Group and Alliance NGR).

Staff is aware that CaliforniaFIRST, which was authorized to operate in Sunnyvale in 2010, does not currently comply with the requirements that staff is proposing. Staff will evaluate the implications, reach out to CaliforniaFIRST to discuss the conditions approved by City Council, and consider whether the City should take further action.

### **FISCAL IMPACT**

There is no direct cost to the City to join the various JPAs in order to sponsor PACE programs. Once operational, there would be a limited amount of staff time dedicated to oversight of the approved PACE providers and coordination with the PACE providers to ensure that information on other energy programs and financial assistance is accurately conveyed. Additionally, staff will create a webpage summarizing the various financing programs that are available so that property owners are aware of all the program options and can shop for the program that best meets their needs. Staff will also integrate information on PACE financing into existing outreach efforts.

### **PUBLIC CONTACT**

Public contact was made by posting the Sustainability Commission agenda on the City's official-notice bulletin board outside City Hall, at the Sunnyvale Senior Center, Community Center and Department of Public Safety; and by making the agenda and report available at the Sunnyvale Public Library, the Office of the City Clerk and on the City's website.

### **ALTERNATIVES**

Recommend that City Council:

1. Approve the proposed operating conditions as presented in Attachment 3 and establish these

conditions as requirements for PACE providers to operate in Sunnyvale.

2. Authorize the City Manager to execute the Adoption of the Association of Bay Area Governments (ABAG) Regional Collaborative Services Agreement with Residential PACE Providers (Attachment 4).
3. Adopt a resolution (Attachment 5) authorizing the inclusion of properties within the City's jurisdiction in the California HERO program and approving an amendment to the Western Riverside Council of Governments (WRCOG) Joint Powers Agreement (Attachment 6) adding the City of Sunnyvale as an Associate Member, and authorize the City Manager to execute the Associate Member Agreement with WRCOG (Attachment 7).
4. Adopt a resolution (Attachment 8) authorizing the inclusion of properties within the territory of the City of Sunnyvale in the CSCDA Open PACE Program for those providers signing the City's Letter of Agreement and the ABAG Regional Agreement.
5. Adopt resolutions (Attachments 9 and 10) authorizing the inclusion of properties within the City's jurisdiction in the Ygrene program through the California Home Finance Authority Community Facilities District No. 2014-1 (Clean Energy) under SB 555 and under AB 811 and approving an amendment to the California Home Finance Authority/Golden State Finance Authority's Joint Powers Agreement (formerly the California Rural Home Mortgage Finance Authority) adding the City of Sunnyvale as an Associate Member, and authorize the City Manager to execute the amendment to the California Home Finance Authority/Golden State Finance Authority's Joint Powers Agreement adding Sunnyvale as an Associate Member (Attachment 11).
6. Adopt a resolution (Attachment 12) authorizing the City to join the FigTree PACE Program, approving Associate Membership for the City in the California Enterprise Development Authority's Joint Powers Agreement (Attachment 13), and authorizing the California Enterprise Development Authority to conduct contractual assessment proceedings and levy contractual assessments within the territory of the City of Sunnyvale, and authorize the City Manager to execute the Associate Member Agreement with the California Enterprise Development Authority (Attachment 14);
7. Authorize the City Manager to execute other documents or agreements necessary to implement the above PACE programs as the City Manager concludes are necessary and appropriate.
8. Find that the Actions are Exempt from Environmental Review under CEQA Guidelines Section 15378(b)(4).
9. Do not join any of the Joint Powers Authorities and do not add additional PACE providers.
10. Other actions as directed by the City Council.

#### **STAFF RECOMMENDATION**

Recommend Alternatives 1 through 8 to City Council:

1. Approve the proposed operating conditions as presented in Attachment 3 and establish these conditions as requirements for PACE providers to operate in Sunnyvale;



2. Authorize the City Manager to execute the Adoption of the Association of Bay Area Governments (ABAG) Regional Collaborative Services Agreement with Residential PACE Providers (Attachment 4);
3. Adopt a resolution (Attachment 5) authorizing the inclusion of properties within the City's jurisdiction in the California HERO program and approving an amendment to the Western Riverside Council of Governments (WRCOG) Joint Powers Agreement (Attachment 6) adding the City of Sunnyvale as an Associate Member, and authorize the City Manager to execute the Associate Member Agreement with WRCOG (Attachment 7);
4. Adopt a resolution (Attachment 8) authorizing the inclusion of properties within the territory of the City of Sunnyvale in the CSCDA Open PACE Program for those providers signing the City's Letter of Agreement and the ABAG Regional Agreement;
5. Adopt resolutions (Attachments 9 and 10) authorizing the inclusion of properties within the City's jurisdiction in the Ygrene program through the California Home Finance Authority Community Facilities District No. 2014-1 (Clean Energy) under SB 555 and under AB 811 and approving an amendment to the California Home Finance Authority/Golden State Finance Authority's Joint Powers Agreement (formerly the California Rural Home Mortgage Finance Authority ) adding the City of Sunnyvale as an Associate Member, and authorize the City Manager to execute the amendment to the California Home Finance Authority/Golden State Finance Authority's Joint Powers Agreement adding Sunnyvale as an Associate Member (Attachment 11).
6. Adopt a resolution (Attachment 12) authorizing the City to join the FigTree PACE Program, approving Associate Membership for the City in the California Enterprise Development Authority's Joint Powers Agreement (Attachment 13), and authorizing the California Enterprise Development Authority to conduct contractual assessment proceedings and levy contractual assessments within the territory of the City of Sunnyvale, and authorize the City Manager to execute the Associate Member Agreement with the California Enterprise Development Authority (Attachment 14);
7. Authorize the City Manager to execute other documents or agreements necessary to implement the above PACE programs as the City Manager concludes are necessary and appropriate; and
8. Find that the Actions are Exempt from Environmental Review under CEQA Guidelines Section 15378(b)(4)

Prepared by: Elaine Marshall, Environmental Programs Manager

Reviewed by: Melody Tovar, Regulatory Division Manager

Reviewed by: Kent Steffens, Assistant City Manager

Approved by: Deanna J. Santana, City Manager

### **ATTACHMENTS**

1. Not Used (for use with report to Council)
2. PACE Provider Comparison
3. Final Draft Letter of Agreement Regarding Operational Requirements for PACE Programs in the

City of Sunnyvale

4. ABAG Adoption of Agreement for Collaborative Services
5. Resolution - HERO/WRCOG
6. WRCOG JPA Agreement (HERO)
7. WRCOG JPA Amendment (HERO)
8. Resolution - Opt-in for CSCDA Open PACE Program
9. Resolution - Ygrene SB 555
10. Resolution - Ygrene AB 811
11. California Home Finance Authority/Golden Station Finance Authority JPA
12. Resolution - FigTree
13. CEDA JPA
14. CEDA Associate Member Agreement