D.13

Contra Costa County

To: Board of Supervisors

From: INTERNAL OPERATIONS COMMITTEE

Date: June 16, 2015

Subject: Property Assessed Clean Energy (PACE) Financing

RECOMMENDATION(S):

1. ACCEPT this report from the Internal Operations Committee on PACE financing; and,

2. DIRECT the Department of Conservation and Development (DCD) to implement an application process to enable PACE financing providers to apply to operate PACE programs in Contra Costa County.

FISCAL IMPACT:

Costs incurred by the County to review and process applications from PACE providers will be reimbursed through an application fee.

BACKGROUND:

Summary

California law allows cities, counties, and other authorized public agencies to establish

☑ APPROVE ☐ OTHER

☐ RECOMMENDATION OF CNTY ADMINISTRATOR ☑ RECOMMENDATION OF BOARD COMMITTEE

Action of Board On: **06/16/2015** ☐ APPROVED AS RECOMMENDED ☐ OTHER

Clerks Notes:

VOTE OF SUPERVISORS

I hereby certify that this is a true and correct copy of an action taken and entered on the minutes of the Board of Supervisors on the date shown.

ATTESTED: June 16, 2015

David Twa, County Administrator and Clerk of the Board of Supervisors

By: , Deputy

Contact: Jason Crapo (925) 674-7722

cc:

voluntary financing districts to facilitate energy and water efficiency improvements to existing residential and commercial properties. Such financing is commonly referred to as Property Assessed Clean Energy (PACE) financing. Once established, property owners within the boundaries of such a district can opt to borrow funds from the district to make energy efficiency improvements, and repay the funds in installments on their property tax bill.

BACKGROUND: (CONT'D)

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Several PACE financing providers have expressed interest in establishing PACE financing districts and offering PACE loans to property owners in Contra Costa County. Such financing districts would not be formed or operated by the County, but the establishment of such financing districts requires a resolution of approval by the Board of Supervisors. The County Treasurer-Tax Collector and County Auditor-Controller would administer collection of assessment payments from property owners through the property tax collection process.

PACE financing has the potential to generate both environmental and economic benefits to County residents, and is consistent with County policy objectives to improve energy efficiency and reduce greenhouse gas emissions. However, the extent of these benefits is yet to be determined because PACE financing is relatively new and the degree to which it might be utilized by property owners within the County is unknown.

Due to regulatory intervention by the federal government to discourage the use of PACE financing, such programs carry potential risks and costs to the County and to property owners that should be mitigated to the greatest degree possible.

On August 14, 2012, the Board of Supervisors referred to the Internal Operations Committee (IOC) an evaluation of establishing PACE districts within the County. The matter was taken up by the IOC in December 2012, but as new information became available regarding legal and federal regulatory issues, Supervisor Mitchoff, who introduced the matter to the Board for study, decided to withdraw her committee referral. The matter was again referred to the IOC on September 9, 2014. The IOC had a lively discussion of the program on November 3, 2014 and requested additional information from staff and PACE Program administrators for future deliberations in March 2015. The IOC received a follow-up report from DCD on March 9, 2015 and, based on the Committee's review, recommends the Board of Supervisors direct DCD to accept applications from entities proposing to form PACE financing districts in Contra Costa County and assess the risks and costs associated with various program proposals in consultation with County Counsel, the County Auditor-Controller and the County Treasurer Tax-Collector. Upon successful completion of such review, PACE financing providers would be required to enter into an Operating Agreement with the County that would establish conditions for operations within the County. The County’s costs of reviewing a PACE program application would be reimbursed by the applicant in the form of an application fee.

District Formation and Property Owner Participation

State law allows for the formation of either Assessment Districts or Mello-Roos Community Facilities Districts (PACE financing districts) for the purpose of financing energy or water efficiency improvements to existing residential and commercial properties. Once established, these districts would raise capital either through selling bonds or securing financing from banks or other private lenders. This capital would be made available to property owners on a voluntary basis to finance energy efficiency improvements on private property.

Once a PACE district is established, property owners within the district's boundary can voluntarily opt into the district by entering into a contract (known as a "contractual assessment") with the public agency responsible for administering the district. The contract would not be with the County, but rather with another public agency. For most current PACE programs, the sponsoring public agency is a joint powers authority (JPA), which forms the financing district and is responsible for its administration. In such cases, the County would need to be a member of the JPA in order for the PACE program to operate within the County.

By entering into a contractual assessment, a property owner would be able to borrow funds from the PACE district to construct energy or water efficiency improvements. This property assessment would be repaid in installments collected by the County Treasurer-Tax Collector on property tax bills.

PACE Has Potential Benefits, but is New and Extent of Benefits is Unknown

PACE financing benefits property owners by providing an additional source of capital to fund energy efficiency improvements. Such lending activity also has the potential to produce indirect public benefits that are consistent with County policy objectives. Improved energy efficiency on private property reduces greenhouse gas emissions and the associated negative impacts of climate change, consistent with the County's Climate Action Plan. Construction of energy and water efficiency improvements on private property also stimulates the local economy, expanding employment and increasing tax revenue for the County.

However, the extent to which PACE financing may generate public and private benefits within the County is unknown. PACE is a relatively new financial product, and the market for the services offered by PACE districts is in its initial stage of development. Furthermore, these districts will be in competition with other established forms of energy efficiency financing, such as equipment leasing and conventional bank lending, that may offer more competitive financing terms.

Prior Action Taken by the County

In 2010, the Board of Supervisors passed a resolution authorizing the formation of a PACE financing district for the CalforniaFIRST program, a partnership between a private financial services firm called Renewable Funding and a joint powers authority called the

California Statewide Communities Development Authority (CSCDA), of which Contra Costa County is a member. CSCDA is a public agency having the legal authority to establish a PACE financing district within the County.

Federal Intervention to Regulate Residential PACE

In 2010, soon after the County adopted a resolution to participate in CaliforniaFIRST, the Federal Housing Finance Agency (FHFA) intervened and took the position that PACE financing represents a form of lending that is detrimental to the mortgage industry, and directed Fannie Mae and Freddie Mac to restrict their purchase of mortgages where PACE districts exist (Attachment A). Fannie Mae and Freddie Mac subsequently stopped purchasing mortgages for properties that have opted into PACE districts (Attachment B).

The federal government's assertion that PACE financing has an adverse impact on mortgage lenders results from the senior lien position of PACE liens over other debts on the property, such as a mortgage or other forms of private lending. The federal government argues that the senior position of a PACE lien undermines the credit value of other debt on a property, such as a mortgage.

FHFA's actions have created negative financial impacts for property owners with PACE loans. Due to FHFA's actions and resulting decisions by Fannie Mae and Freddie Mac to cease purchases of mortgages for properties with PACE liens, some home owners have been required to pay off their PACE loans in order to obtain new mortgage financing on their property, as is typically necessary to sell a home or refinance an existing mortgage.

State and Federal Officials in Continuing Disagreement Regarding PACE

Shortly after FHFA intervened to regulate residential PACE lending in 2010, the State of California and several local jurisdictions, including Sonoma County, litigated against the federal government over its regulatory intervention into this area, arguing that FHFA had not followed the required rule-making process for establishing such regulation. The State ultimately lost this lawsuit in federal court in 2013.

Failing to overturn FHFA's position in court, the State has subsequently attempted to address FHFA's concerns regarding the negative impacts of PACE on the mortgage industry by establishing a PACE Loss Reserve Program to insure mortgage lenders against financial losses resulting from PACE liens (Attachment C). The creation of California's PACE Loss Reserve Program has resulted in renewed interest in residential PACE lending throughout the state. However, despite these efforts, FHFA remains opposed to residential PACE lending and continues to prevent Fannie Mae and Freddie Mac from purchasing mortgages on properties with PACE liens. This position was reiterated in a recent letter from the Director of FHFA to Governor Brown (Attachment D).

The ongoing dispute between the State of California and FHFA places local jurisdictions that implement residential PACE programs at risk of potential negative action by FHFA. The magnitude of this risk is unknown. However, FHFA's General Counsel has recently sent letters to County Counsels in California, such as the County Counsel for Santa Clara County (Attachment E) requesting that counties participating in PACE disclose the potential adverse implications of PACE loans to property owners.

Review of PACE Applications by the County

Ongoing efforts by FHFA to discourage mortgage lending on residential properties with PACE loans require the County act prudently in considering the formation and operation of PACE financing districts. Each proposal to form such a district should be reviewed by County staff to minimize the public's exposure to the risks and costs associated with these programs.

To this end, the Internal Operations Committee recommends that PACE programs interested in operating within the County be required to submit an application that would be reviewed by County staff. A copy of the proposed PACE Application form is attached to this Board Order (Attachment F). DCD would serve as the central point of contact for applicants and would work closely with other County departments in the review of applications, including County Counsel, the County Auditor-Controller and the County Treasurer Tax-Collector. DCD will collect an initial deposit of $5,000 to pay for County staff time and other costs incurred by the County in reviewing applications. Any portion of the deposit not spent will be returned to the applicant at the conclusion of the application process. Staff may seek additional reimbursement of application processing costs from program providers if such costs exceed the initial $5,000 application fee deposit.

Following a satisfactory review of application materials, PACE providers will be required to enter into an Operating Agreement with the County, in a form substantially similar to the one attached to this Board Order (Attachment G). The Operating Agreement requires PACE providers participate in the State's PACE Loss Reserve Program, disclose potential financial risks to borrowers, including risks resulting from federal regulatory actions, and indemnify the County from claims that may arise from operation of the PACE program within the County. Such conditions are intended to protect the interests of the County and property owners in light of ongoing federal opposition to PACE. Other conditions may also apply based on staff review of application materials. The Operating Agreement and other documents requiring Board approval to implement the PACE program would then be submitted to the Board of Supervisors for consideration.

CONSEQUENCE OF NEGATIVE ACTION:

Without Board approval, PACE financing would not be available to homeowners in Contra Costa County.

CLERK'S ADDENDUM

Speakers: ***Jonathan Kevles, Renew Financial, and Program Administrator for the CaliforniaFIRST PACE Program; Mitch Smith, Solar Technology Builders; William L. Noack, HERO program; Eve Perez, HERO program.***

County Counsel noted that a disclosure for the homeowner of the lien on the property is included in the operating agreement between the installer and the homeowner. Supervisor Piepho requested it also be included in the permitting process to ensure the homeowner has clear understanding about the priority order of repayment of the loan (a senior lien), in the event the property owner desires to take such actions as sale of the property or refinancing of the mortgage; Supervisor Andersen noted that Riverside County District Attorney's office has opened an investigation into a PACE program provider for suspected predatory lending practices. She requested staff reach out to Riverside County to obtain further information on the status of that. The Board discussed the valuation of the property using the amount listed on the Assessor's tax roll versus the fair market value. The current proposal is based on the assessed value of the property. It was noted other jurisdictions use whichever value is greater. The Board expressed great concern about the risk of exposing the property owner to predatory lending practices. It was noted that the policy to use the more conservative basis of assessed value can be amended at a later date. The Board will move forward with the program in its current form to prevent delay in the implementation. The Board ADOPTED the recommendations as presented today; DIRECTED the Conservation and Development Department to return to the Board at the last meeting in December 2015 with a report on such items as the actual staff cost of processing the application, how many applicants did or did not qualify, and any other pertinent statistics available.

ATTACHMENTS

Attachment A: FHFA 2010 Position Letter on PACE

Attachment B: Fannie Mae 2010 Announcement Regarding PACE

Attachment C: CA State PACE Loss Reserve Program

Attachment D: 2014 FHFA Letter to Gov. Brown

Attachment E: 2014 FHFA Letter to Santa Clara County Counsel

Attachment F: Proposed Contra Costa County PACE Application Form

Attachment G: Proposed Contra Costa County PACE Operating Agreement