

NEW FINANCING PROGRAM IS RAISING THE PROSPECTS FOR GREEN ROOFS

BY ERIC J. ALINI

In the past, the higher upfront costs of green roofs over conventional roofing often stopped projects before they started. But no longer. Green roofs can now effectively compete with conventional roofing through a new type of financing that covers the cost of eligible energy efficiency, sustainability and resiliency projects.

Through a public-private partnership, Property Assessed Clean Energy (PACE) incents owners to make energy efficiency upgrades by providing 100% financing that is long term, fixed rate and preserves the property owner's capital. Owners may even elect to defer the first payments by including capitalized interest in the financing - allowing rental income to stabilize before repayment begins and aligning the ongoing utility savings with repayment costs for the improvements. Prepaid service and warranty contracts may be included, lowering maintenance costs as well. By including irrigation, elevators, stairs and related roofing work in the financing, green roofs can now be installed with no upfront capital and have become economically attractive.

Since 1736, when Benjamin Franklin proposed the idea of property tax to pay for the Philadelphia fire department, tax assessment financing has funded public service projects - from new sidewalks to schools. Today, PACE is the nation's


first voluntary property tax assessment applied to individual buildings. It's an innovative way to pay for reducing the environmental footprint of America's building stock by helping owners reduce their upfront costs through property tax assessment financing. For projects that typically can't calculate energy savings or offer payback periods that are too long for conservative investors, PACE transforms the standard return on investment (ROI) model and provides a unique set of positive economic incentives that make environmental upgrades such as green roofs very attractive.

The PACE financing mechanism begins when funds are transferred from a capital provider to a government agency. Funding is then secured through a tax assessment placed on the building and repaid through the property tax bill. As a result, the repayment of the financing is treated as a tax on the property rather than a loan expense, greatly improving a project's economics.

PACE GREEN ROOF CASE STUDY

- Project Cost: \$350,000-Green Roof design, engineering and installation, irrigation, horticultural design and installation
- Related Costs: \$150,000-Stairway to roof, permits & inspections, Prepaid service contract, Roofing structural and membrane work
- Total Costs to be financed: \$500,000
- Terms: 25 years at 7% fixed rate interest, no balloon
- Estimated annual assessment added to property tax bill: \$49,500 -\$4,125 pro rated monthly cost
- Pass-through to tenants depends upon lease; stormwater management and energy savings varies with each individual property

Source: Green Roof Program, www.counterpointesre.com



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SPLIT INCENTIVE

PACE is the long-awaited solution to the commercial building sector's greatest barrier to environmental best practices: the split incentive. Split incentive relates to commercial real estate lease language obligating a tenant to pay for utility costs and a landlord to pay for building upgrades. Building owners, carrying all the costs of the upgrade and passing all the energy savings to the tenants, may never see a positive return on the investment. So it's not surprising that Lawrence Berkley National Lab's 2013 "Remaining Market Potential of the U.S. Energy Services Company Industry" found commercial buildings lag behind all other building segments with a pitiful 10% adoption rate of energy efficiency technologies. PACE solves the great split-incentive dilemma by converting project financing to property tax assessment financing. This triggers an accounting transformation with considerable benefits. Under most commercial leases, tenants pay the utility bills and the property tax, placing them with de facto responsibility for repaying the cost of projects while benefiting from lower utility bills- closing the split-incentive gap.

Now commercial building owners can access low-cost, private sector capital to pay for 100% of eligible projects, finance the cost of the project over time to ensure that the annual payments are less than the annual utility savings, and avoid split-incentive. On top of that, debt liability may not be impacted if the financing receives off-balance sheet treatment. The building is improved without any capital expenditure and operating expenses are reduced.

THE PPA MOMENT FOR GREEN ROOFS

Could PACE be the special ingredient that makes green roofs commonplace? There is precedent. Before Power Purchase Agreements (PPA) were introduced to the solar industry, rooftop solar was a luxury consumer product. The advent of the PPA made solar energy an economically attractive option for building owners. PACE financing may have the same transformative power on the green roof industry.

As markets learn to use PACE at a meaningful scale, its impact will be felt across industries. Already, the earliest signs of disruption can be seen. Contractors who quickly learned the basics of PACE are starting to grab market share by offering a solution that sets them apart.

PACE is still in its infancy, having only developed the public sector infrastructure necessary to handle the cash streams over the last 3 to 5 years. Its potential is clear with early signs of exponential growth. Rocky Mountain Institute promotes it - Lawrence Berkeley National Labs validates it - and Scientific American magazine calls it a top 20 "world changing" idea. Red and blues states across the country are passing legislation to enable it, making PACE financing the fastest growing financial tool in the U.S. As PACE goes mainstream, vendors who align with this tool will emerge as new industry leaders and products once thought to be luxuries will become the new standard. Green roofs should be one of those standards emerging as the new norm for America's buildings.

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