Financing Programs for Energy Efficiency: Utility Roles

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Why Financing??

- Cost effectiveness tests are getting more challenging.
- Ratepayers are getting more sensitive to higher rates.
- EE goals are getting more aggressive in some places.
- The trend away from CFLs may require more focus on attached fixtures w/larger investment upfront.
- Rebates and tax incentives may not be the most cost effective way to do the job.
  - Leveraged, private capital may be much more effective. IF it is designed effectively.
Almost no one wants financing.

But people want the stuff that financing lets them buy (granite countertops, furnaces, cars, homes…)

So: market energy efficiency. Make financing seamlessly easy to access.

Financing programs need to be tightly integrated into every other element of marketing, rebates, etc.
Capital Sources
- Banks
- Credit Unions
- CDFIs
- Bonding
- Federal
- Other (Treasury)
- Utilities

Who Lends?
- State - energy office
  - HFA
- Utility
- Finance company
- Bank
- Credit Union
- CDFI

Security
- Tax lien
- Fixture lien
- At the meter
- Unsecured

Enhance
- Loss Reserve
- Debt Service Reserve
- Loan Insurance
- Sub Loans

Lend

Repay
- On Bill
- Property Tax
- Other Fee
- 3rd Party

3rd Party Security
- Tax lien
- Fixture lien
- At the meter
- Unsecured

Other Fees
- Tax lien
- Fixture lien
- At the meter
- Unsecured
Everything starts with the source of capital.

Flexible capital that can be put at risk can be used to:

1. make loans to below-typical credit quality borrowers.
2. make loans for extended periods (eg. 15+ years in residential programs)
3. provide financing where the obligation to pay stays with the meter
Leverage

Credit enhancements

- Money that a utility sets aside to cover potential losses that a lender might incur, up to some maximum amount.
- If losses are less than the amount of the credit enhancement then the utility gets its funds back or the funds can be used to support additional lending.
- If losses are greater than the size of the credit enhancement, the lender bears the loss.

- Ratepayers/shareholders funds are leveraged by a multiplier (5% reserve = 20x leverage) while capping the amount of ratepayer/shareholder exposure.
Lending Regulations
- Q: What are two of the most highly regulated industries in the country?
- A: Utilities and Financial Services
- Most utilities will think hard before deciding to take on financial regulation.
  - Truth in Lending Act (TILA)
  - Consumer-finance laws

Billing Systems, Payment Tracking
- What happens with partial payments?
- Are your billing systems set up to run financing programs?
The Spectrum of Utility-Based EE Financing

On Bill Finance (utility bill/utility capital) → On Bill Invoice (utility bill) → 3rd Party Bill (Utility Capital) → 3rd Party Bill (Utility Credit Enhanced)

Move to the right and the utility role diminishes while non-utility role increases.

“Utility” could be shareholder or ratepayer funds.
Utility On Bill Financing: MidWest Energy

- Tariff-based; obligation passes with meter.
  - 3% for most loans.
  - 15 years for residential.
  - 10 years for commercial.
  - Capital source: utility, ARRA.
  - Disconnection for failure to pay.
  - Financing charges cannot exceed 90% of average annual energy savings.
  - About 500 projects completed worth $2.5 million.
  - 0 defaults as far as known.
Utility Invoicing–Only

Utility Invoicing
- Set up so that utility does not provide capital, but only bills on behalf of a 3rd party lender.
- Since the utility is not the creditor, it should avoid regulation under TILA.
- One variant is to have two EFT payments (one for lender and one for utility bill).
- Under consideration in Indianapolis (IPL).

3rd Party Billing w/Utility Capital
- Not aware of any such programs in operation.
Utility provides funds to cover loan defaults up to a certain level.

- Typical levels for residential lending are 5%-10%, depending on credit quality.
- In exchange, lender offers a reduced interest rate, longer loan term or broader access to capital (relaxed underwriting standards).

Multiple programs in operation or under development (not always with utility funds).

- Michigan Saves, Keystone HELP.
- UniSource-filed finance program uses this model, as does APS.
Michigan Saves

- $60 million loan facility based on $3 million loan loss reserve.
- 7% rate to borrower.
- 10 year max loan term.
- 640 and a higher FICO score required (about 50% of MI population qualifies).
- Marketed through a contractor network.
- Launched a couple of weeks ago.
  - 50% approval rate. About 25 loans made.
Utilities cover defaults on loans (but do not originate or service loans).

Participating banks offer a 5% loan with a minimum FICO score of 650.

Loan terms up to 24 months for small loans (up to $2,000).

Terms go to 7 years for loans up to $15,000.

Loan products for large residential and large C&I under development.

Negotiations conducted directly with the Mass Bankers Association.
Illinois Utilities

- Legislation required utilities to develop efficiency financing programs -- $2.5 million each utility for a statewide total of $12.5 million.
- Utility ratepayers would cover 100% of defaults.
- A 3rd party entity conducts all loan origination and servicing. Capital source is still uncertain. Loan terms TBD. Contract awarded but not public.
- Program size is limited to $12.5 million statewide.
Conclusions

- Utility funds can be used to provide leverage to attract private capital.
- Financing program options exist that allow utilities to support lending – but not originate loans.
- Finance program options exist that allow utilities to avoid exposure to lending regulations.
Conclusions

- Loan programs can work, if they are streamlined and marketed not just as financing but as a means to better equipment, more energy savings.
- Financing is part of the key to meeting ambitious efficiency goals while balancing cost effectiveness tests.