

Commercial Solar Market Picks Up the PACE

A new form of financing could help spur investor interest in green energy developments in commercial real estate projects.

By Carol J. Clouse



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The U.S. residential solar installation market has grown substantially over the past few years, leaving small-scale commercial solar lagging behind. The market for solar panels on commercial buildings has failed to gain traction largely because it has lacked three things: a way to assess credit, standardized documentation and motivation on the part of commercial real estate owners.

The commercial solar market, however, is poised to kick up some dust of its own in 2015, thanks in part to a newish form of financing that opens up a broader set of opportunities for institutional investors looking to invest in solar. Dubbed property-assessed clean energy (PACE) financing, such programs are used to pay for both renewable energy and energy-efficiency projects.

With residential solar, developers have used homeowners' FICO scores to determine creditworthiness. There is no commercial equivalent. PACE solves this problem because it's secured through a special tax assessment, so it's much easier for a business owner to be approved for the loan.

"We've gotten numerous calls from churches, car dealerships and other businesses," says Anthony Fotopoulos, based in Denver and Americas CEO for Hamburg, Germany-headquartered solar energy

company Conergy, which is working on a commercial PACE program in California. "Their credit is not going to work for an institutional-type investor, but if you do some type of a PACE financing, where you're just looking at the mortgage and the equity on the property underneath, you know that you're covered. It opens up a huge segment of the market."

The first PACE initiative was introduced to the residential market in Berkeley, California, in 2008, but the program suffered setbacks and only began gaining steam again in 2013. The first residential PACE securitization was priced in early 2014 — a \$104 million deal led by Deutsche Bank for the Western Riverside Council of Governments in Riverside, California. In October WRCOG sold its second round of residential PACE asset-backed securities — a slightly bigger transaction, at \$129 million.

Lawmakers in roughly 30 states have passed legislation that allows for commercial PACE programs. Nearly ten of those states have programs up and running, with California and Connecticut leading the way in terms of scale, as the commercial PACE securitization market is just getting ready to take off, say industry insiders.

“If you think of it like a pot of boiling water, we’re at that point where there are bubbles on the side and steam rising,” says Haresh Patel, CEO of Mercatus, a developer of solar energy investment tools headquartered in San Jose, California. “We’re getting pretty close.”

In May Sausalito, California–based Clean Fund, which provides commercial building owners with funding for [energy efficiency](#), water efficiency and [renewable energy](#), purchased roughly \$30 million worth of commercial PACE loans from the Clean Energy Finance and Investment Authority, Connecticut’s green bank. John Kinney, founder and CEO of the specialty finance company Clean Fund, expects to see the first commercial PACE securitization this year.

“Until recently, commercially distributed generation has only been available for investment-grade credits, such as the municipal, university, schools and hospitals sector,” he says. “That represents about 15 percent of the total market.” PACE can open the market to credits that are below investment-grade, which make up the vast majority of commercial real estate used by smaller businesses, such as shopping centers, office parks and warehouse facilities.

PACE should also help to streamline the documentation process for commercial solar deals, because the power purchase agreements are written at the municipal or county level, and the paperwork remains the same with every transaction. “In all the 50-plus [non-PACE] deals that we’ve done, I’ve never done a commercial-scale deal where there’s not something changed,” says Conergy’s Fotopoulos. “So when you try to securitize, you’ve got 100 or 1,000 different documents. How do you do diligence on that?”

Finally, PACE should help motivate commercial property owners to install solar panels because there are no up-front costs. (Building owners historically have been reluctant to invest in something that will, in the short term, benefit only existing tenants.) There’s the added bonus that the special tax assessment owners receive is transferrable if the property is sold.

Fotopoulos says that Conergy is looking at another couple of years for its PACE program to reach enough scale to interest institutional investors: “But if this works, and we think it will, it could be a very interesting segment of the market.”