



NW Energy Coalition

Realizing the Power of Efficiency

Barriers, Opportunities & Solutions to Financing Energy Efficiency for Small and Mid-sized Businesses in the Northwest

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IN PARTNERSHIP WITH

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■ ■ ■ ■ About NW Energy Coalition

The NW Energy Coalition is an alliance of more than 100 environmental, civic, and human service organizations, progressive utilities, and businesses in Oregon, Washington, Idaho, Montana, Alaska, and British Columbia. NWECC promotes development of renewable energy and energy conservation, consumer protection, low-income energy assistance, and fish and wildlife restoration on the Columbia and Snake rivers.

■ ■ ■ ■ Acknowledgments

This report was prepared by Cascadia Consulting Group with the support of Seattle Northwest Securities and Shorebank Enterprise Cascadia. Christine Grant served as principal researcher. Ann Grodnik, an investment banker with Seattle Northwest Securities, and Rachel Brombaugh, a lending specialist with Shorebank, contributed their expertise in financial markets and lending practices to smaller businesses, respectively. Marc Daudon served as Principal in Charge for this project, with oversight and input by NW Energy Coalition project manager John Healy and other Coalition staff.

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Executive Summary

The NW Energy Coalition commissioned this study to identify and find ways to overcome barriers—including lack of capital—to financing energy efficiency projects in the Northwest, specifically the states of Idaho, Montana, Oregon, and Washington. The report focuses on understanding the financing needs of small to medium-sized businesses with fewer than 500 employees. These businesses represent a major share of the regional economy and energy use but generally have lower participation rates in existing energy efficiency programs than larger businesses. As our region plans to meet its growing energy needs, energy efficiency consistently rises to the top as the most cost-effective solution for the Northwest. According to the Northwest Power and Conservation Council, the commercial sector offers the potential for about 1,400 average megawatts through efficiency gains over the next 20 years, nearly two-thirds of which will come from improved lighting systems.

Aside from utility incentives, financing for energy efficiency projects for small to medium-sized business sector is extremely limited. This report explores the current financing marketplace in the Northwest, examining its status, constraints, and opportunities for financing commercial-sector energy efficiency improvements. It identifies current programs that can help address the financing gap, and it makes recommendations for future enhancements to foster energy efficiency lending. The report seeks to answer this core question: **What steps are needed to increase the flow of commercial capital in the small and mid-sized commercial market to achieve energy efficiency on the scale envisioned by Northwest utilities and power planners?** To do so, the report examines key findings and barriers, reviews current programs, identifies potential solutions, and recommends a path forward.

The research team interviewed and examined key current and potential players in the energy efficiency lending marketplace, including lenders and investors (banks, credit unions, venture capitalists, and economic development organizations); public and investor-owned utilities; policymakers and government agencies; energy service companies and other vendors; as well as nongovernmental organizations and other regional energy efficiency experts.

■ ■ ■ ■ Key Findings

The research and interviews identified the following key findings regarding the current energy efficiency financing marketplace and major industry players.

1. Overall demand for energy efficiency financing is currently limited, and accordingly, demand for energy efficiency financing from small and medium-sized businesses is also limited.
2. Markets for lending and energy efficiency services are highly complex and segmented.
3. In the current economy, lending to small and medium-sized businesses is limited for anything, including energy efficiency projects.
4. Financing institutions generally are not focused on energy efficiency lending as a special or significant business opportunity.

5. Lending for energy efficiency to the commercial sector brings its own set of risks.
6. Some financial institutions are actively seeking opportunities in this field and are pioneering innovative lending programs.
7. ESCOs and related vendors are leading the way to secure financing for energy efficiency investments using both private equity and conventional lending.
8. Utilities provide substantial funding for energy efficiency, but generally do not see issuing and servicing loans to their customers as a business opportunity.
9. Trade allies occupy a central place in the network of business owners, contractors, utilities, and lenders, suggesting an important role in promoting financing for energy efficiency.
10. Efforts to create a secondary capital market for energy efficiency loans are in their infancy.
11. Interest in legislation that enables energy efficiency loans to remain with the property—rather than the property owner—is growing in the Northwest.

■ ■ ■ ■ Key Barriers

Multiple barriers limit energy efficiency financing, including the severely weakened economy and financial sector, the relatively poor creditworthiness of many smaller businesses, limited demand for such loans from businesses, and a series of specific challenges associated with establishing collateral for and the near-term financial viability of some energy efficiency investments. In addition, many small businesses share energy use and billing with landlords, splitting costs and benefits and complicating transactions. Finally, the environmental benefits of energy savings are not currently monetized. These barriers mean that for most businesses, lending institutions, and investors, returns are too low and perceived risks are too high for energy efficiency investments to occur on a scale commensurate with either their potential or the need. Accordingly, this marketplace lacks both sufficient liquidity and capital.

■ ■ ■ ■ Current Programs

Despite these challenges, financial institutions, utilities, energy efficiency service providers, and governments are undertaking a number of innovative programs and initiatives to advance energy efficiency lending. Efforts include **credit enhancement** programs that provide loan guarantees as well as **public loan** programs that offer financing or cover a portion of the financing in partnership with a private lender. These initiatives point the way forward, providing new approaches and solutions to increase capital flows for energy efficiency projects.

■ ■ ■ ■ Options for Increasing Energy Efficiency Lending

A portfolio of solutions will be needed to address the barriers and increase energy efficiency financing across the diverse spectrum of small to mid-sized businesses. The following table summarizes 15 potential solutions to increase energy efficiency financing in the Northwest. The checkmarks indicate that **the option reduces risk, increases demand and improves return, or increases liquidity and capital flows to financial institutions or lenders.**

Summary of Proposed Solutions to Increase Energy Efficiency Financing in the Northwest

CATEGORIES AND OPTIONS	Mitigates Risk for Lenders	Increases Demand/ Return to Lenders	Provides Liquidity/ Capital
IMPROVEMENTS TO THE PERFORMANCE OF EXISTING FINANCE MECHANISMS			
1 Encourage utilities to adopt on-bill repayment mechanisms.	✓		✓
2 Encourage utilities to provide progress payments to businesses that qualify for energy efficiency rebates and incentives.		✓	✓
3 Dedicate a portion of existing Small Business Administration lending to energy efficiency projects.			✓
4 Accelerate the development of secondary markets for energy efficiency loan portfolios.	✓		✓
IMPROVEMENTS TO EXISTING ENERGY EFFICIENCY FINANCING SUPPORT SERVICES AND SYSTEMS			
5 Accelerate the adoption of commercial building energy performance tracking and disclosure.	✓	✓	
6 Facilitate information sharing among utilities, financial institutions, and contractors about energy efficiency opportunities and cost savings.	✓	✓	
7 Create a utility-sponsored technical assistance program for lenders.	✓	✓	
8 Launch an education and marketing campaign to small and medium-sized businesses to build demand for energy efficiency projects and associated financing.		✓	
9 Promote trade ally networks and “one-stop shopping” for energy efficiency resources to small and medium-sized businesses.	✓	✓	✓
LEGISLATIVE AND REGULATORY CHANGES AT THE FEDERAL OR STATE LEVEL TO ALTER THE MARKETPLACE			
10 Advance Property Assessed Clean Energy (PACE) financing in Washington, Idaho, and Montana—similar to Oregon’s existing law.	✓	✓	✓
11 Provide utilities with more incentives and fewer barriers to invest their resources in deep energy efficiency retrofits.		✓	
12 Support federal legislation to permit tax-exempt bond financing for clean energy and energy efficiency.		✓	✓
NEW PROGRAMS AND INSTITUTIONS TO ADD CAPACITY			
13 Create a federal Clean Energy Deployment Administration or “Green Bank.”	✓		✓
14 Use municipal, state, or federal bond-issuing authority to raise funds for energy efficiency projects.			✓
15 Develop and expand revolving loan funds to support energy efficiency projects.	✓		✓
16 Expand credit enhancement and other mechanisms that leverage private capital.	✓	✓	✓

■ ■ ■ ■ Recommendations

Each of these solutions, if implemented, has the potential to strengthen the marketplace for energy efficiency financing, but **which options should be pursued and in what priority order to increase financing of energy efficiency projects for small and medium-sized businesses in the Northwest?** The report's conclusion recommends priorities for early action. These recommendations are intended to lay the foundation for further change and help the marketplace function better on its own to drive energy efficiency action.

For near-term action, we recommend several solutions that stand out in their potential to leverage resources, stimulate change in the marketplace, engage lenders, and consequently lead to rapid growth in financing for energy efficiency.

- **Early action #1.** Market existing energy efficiency programs more effectively through coordinated efforts of governments, utilities, and organized trade ally networks. This effort includes collection and dissemination of better information about the performance and financial benefits of energy efficiency upgrades for businesses. We recommend doing so through 1) widespread adoption of the U.S. Environmental Protection Agency's Energy Star portfolio manager or an alternative standardized rating system to track a building's energy performance and 2) implementation of a utility-sponsored Energy Conservation Advisor program for lenders.
- **Early action #2.** Advance Property Assessed Clean Energy (PACE) financing legislation where feasible, providing the basis for emergence of a secondary market for energy efficiency loans, benefiting both commercial and residential sectors.
- **Early action #3.** Encourage utilities whose billing systems have been upgraded to enable on-bill repayment to use this mechanism to facilitate and increase lending for energy efficiency projects, reducing upfront capital contributions required from businesses, simplifying loan repayment, and making a direct connection between energy and cost savings for the customer.
- **Early action #4.** Provide utilities with more incentives and fewer barriers to invest their capital and human resources in comprehensive, deep energy efficiency retrofits throughout their service markets.
- **Early action #5.** Establish public energy efficiency funds dedicated to offering credit enhancement to leverage private capital through the use of available municipal, state, and federal funds, including bonds.

Together, these solutions can provide a catalyst for lenders and investors to finance energy efficiency. They can serve to reduce risks for banks and investors (transferring risk to government or utilities in some cases), increasing returns to borrowers and lenders, boosting liquidity and capital flows—and helping secure the Northwest's clean, efficient energy future.