California Housing Partnership Corporation
California's Experts on Affordable Housing Finance, Advocacy & Policy

California Energy Commission
DOCKETED
12-EBP-1
TN # 67994
OCT. 23 2012

October 23, 2012

Commissioner Andrew McAllister
California Energy Commission
Dockets Office, MS-4
1516 Ninth Street
Sacramento, CA 95814-5512

Re: Docket Number 12-EBP-1 -- AB 758 Scoping Report Staff Workshop Written Comments

I am writing on behalf of the California Housing Partnership Corporation (CHPC) to provide comments on the AB 758 Scoping Report. I thank the Commission for inviting me to present on a panel at the October 8th staff workshop and for the opportunity to further contribute to the public record with written comments.

CHPC is a statewide organization dedicated to assisting nonprofit and government housing agencies to create, acquire, green, and preserve housing affordable for lower-income households, while providing leadership on housing preservation policy and funding. CHPC is also the convener of the Green Rental home Energy Efficiency Network (GREEN), a coalition of more than 40 organizations committed to increasing access to energy efficiency resources for low income residents of multifamily rental properties in California and ensuring that these resources are used as effectively as possible to achieve deeper energy savings consistent with the California Long Term Energy Efficiency Strategic Plan[1].

The Strategic Plan states a target of 30 percent reduction in existing home energy purchases of 75 percent of all existing homes by 2020, or 1.2 million homes annually. However, the current whole house retrofit program has only accomplished roughly 1,000 upgrades per year[2] none of which have been multifamily. Lowering the barriers to energy efficiency retrofits and financing in multifamily buildings is critical to reaching the state's goals. CHPC is currently facilitating a whole building retrofit of a 274-unit property in Southern California that demonstrates how the delivery of existing rate-payer low income and general efficiency programs can be integrated and combined with On Bill Repayment financing. This one project will result in the upgrade of 274 rental homes for low-income families with an estimated overall savings of 22%.

[1] "CA Energy Efficiency Strategic Plan – January 2011 Update"

[2] California Energy Commission Staff Report, "Comprehensive Energy Efficiency Program for Existing Buildings Scoping Report," Pg. viii.

MAIN OFFICE
369 Pine St.
Ste. 300
San Francisco, CA 94104
Tel: (415) 433-6804
Fax: (415) 433-6805

LOS ANGELES
800 South Figueroa St.
Ste. 760
Los Angeles, CA 90017
Tel: (213) 892-8775
Fax: (213) 892-8776

SACRAMENTO
5325 Elkhorn Blvd.
PO Box 8132
Sacramento, CA 95842
Tel: (916) 683-1180
Fax: (916) 682-1194

SAN DIEGO
113 West G St.
PO Box 319
San Diego, CA 92101
Tel: (858) 693-1572
Fax: (213) 892-8776

Multifamily housing of five or more units provide homes to approximately 3.2 million of the state's 13.7 million plus households[3]. State, federal and local governments have played an essential role in creating and maintaining the long-term affordability of more than 600,000 of the state's multifamily rental homes serving California's lowest income families.

My testimony spoke to four question areas, which I will elaborate on somewhat in these written comments:

I. What makes multifamily rental housing more difficult to retrofit?
II. What are the essential elements of a successful retrofit program?
III. What financing tools have been tried and are not working well?
IV. What are the most promising solutions in development?

I. What Makes Multifamily Rental Housing More Difficult to Retrofit?

There are three main factors that make energy efficiency more difficult to achieve in multifamily buildings compared to single family dwellings:

1. **Larger Buildings with Complex Utility Systems**: Utility systems in multifamily buildings are more complex, require higher skilled labor to retrofit/replace and transcend the division between private living space and common areas. Multifamily buildings typically have common irrigation systems, large exterior lighting systems, large common areas with significant lighting and heating and ventilation loads. But, as has been well documented by many sources including the EPA sponsored California Home Energy Retrofit Coordinating Committee "the single largest and most consistent opportunity in multifamily housing is reducing the energy consumed to heat domestic water." The MF HERC goes on to add that "It is common for multifamily buildings to have central water heaters, typically gas appliances with a large distribution system and recirculation loop."[4] Energy retrofit costs for these more complex buildings typically range between $3,000 and $5,000 per unit with replacement costs typically in the range of $150,000-$400,000. While the retrofit cost is relatively small compared to the value of these buildings, it becomes a barrier during the relatively long period in between refinancings and major renovations, a period that can range from 15-30 years. Due to the loss of state redevelopment and bond funds and related financing challenges, the typical length of time between major renovations is currently lengthening from 15-20 years to 20-30 years. Waiting for these owner-initiated rehabs to make energy efficiency improvements will make it difficult for the state to achieve its goals. [See point #4 below for more detail.]

2. **Split Incentives**: Utility payments in multifamily buildings are typically divided between the building owner and renters, meaning that savings are also split, leading to what is called the "split incentive" challenge where owners must take responsibility for making improvements even though tenants typically control the majority of the savings. Even when owners control a majority of the potential savings, owners are often in contract or

[3] "Selected Housing Characteristics", U.S. Census Bureau, 2011 American Community Survey, 1- Year Estimates.

[4] Multifamily Subcommittee of the California Home Energy Retrofit Coordinating Committee (MF HERCC), "Improving California's Multifamily Buildings: Opportunities and Recommendations for Green Retrofit & Rehab Programs," Pg. 20.

regulatory agreements that require them to pass along any savings to a federal, state or local agency. The Scoping Report states that "affordable housing owners are more capable of overcoming this barrier than market rate housing owners and developers" and the Report points to the California Utility Allowance Calculator as the way to overcome the split incentive issue.[5] We disagree with this conclusion for the following reasons: 1) utility allowances are often not adjusted in a timely manner; 2) for the CUAC to work requires informed owners with the time and motivation to a) conduct the necessary analysis, and b) persuade the local housing authority and regulatory agencies with jurisdiction over rent and utility calculations that the CUAC results should be adopted for the particular property; and 3) for many properties funded through U.S. Department of Housing and Urban Development (HUD) programs, increased income resulting from decreased utility allowances must be passed through to HUD. In recognition of the need to find ways to address the split incentive challenge, the CPUC recently directed utilities to develop and implement On Bill Repayment (OBR) pilot programs in 2013 for low income multifamily properties in particular. OBR has the potential to address the split incentive challenge by tying the repayment tariff to tenant meter as well as owner meter. The pilot phase will begin by using OBR to finance owner meter savings until placing repayment on tenant meters is approved by the CPUC with appropriate protections for low income tenants.

3. **Multiple Financing Layers and Restrictions:** Most multifamily rental buildings serving low income households are financed with multiple layers of debt and equity (the Financing Stack), requiring owners wishing to finance relatively small $3,000/unit retrofits on multi million dollar properties to negotiate with and obtain permissions from numerous parties. In the case of rent restricted rental housing, there are often more than a dozen lien holders whose permission is required to add additional secured financing no matter how small the amount. Rents and cash flow are highly regulated, meaning that in most cases retrofit costs cannot be passed on to tenants. As a result, many

4. **Longer periods between energy retrofits:** The Scoping Report suggests that the ideal time for an energy efficiency retrofit is when a low income property owner recapitalizes every 12-15 years.[6] We disagree with this conclusion for several reasons. First, while the expiration of the 15-year compliance period for the state's 3,285 Low Income Housing Tax Credit (LIHTC) properties typically does trigger a refinancing of some kind in years 12-16, these refinancings are generally very limited in scope and do not contemplate funding significant retrofits that can be easily folded into the new financing. Second, with the loss of Redevelopment Tax Increment Financing and the exhaustion of the last state housing bond (Proposition 1C); overall funding levels for low income multifamily housing have declined by more than 50% in the past three years, effectively lengthening the period before which a substantial rehabilitation is typically undertaken from 15-20 years to 20-30 years. With such long cycles it is important for affordable housing properties to perform energy efficiency retrofits outside of the traditional refinance and substantial rehabilitation cycle. For this reason, we believe the Scoping Report should be amended to reflect this new reality.

---

[5] California Energy Commission Staff Report, "Comprehensive Energy Efficiency Program for Existing Buildings Scoping Report," Pg. 28.

[6] Ibid. Pg. 26.

II. What are the Essential Elements of a Successful Retrofit Program?

There are six main elements that we have learned are essential for successful energy efficiency programs for low income multifamily buildings:

1. **Incentives and Financing Must be Combined**: Because of restrictions on rents that keep them affordable combined with the split incentive problem, most multifamily properties dedicated to serving low income families cannot finance more than about half of the cost of the typical energy retrofit. This means that it is essential that rate payer and government efficiency incentives continue to be offered to these properties at their maximum level.

2. **One Stop Shop Access to Incentives is Critical:** The current fragmented array of rate-payer and other energy efficiency incentives is highly inefficient for multifamily buildings to access and is a major barrier to their participating in these programs. The CPUC recently recognized this point in requiring that the state's Investor Owner Utilities offer a single point of contact to owners accessing their Energy Savings Assistance Program (ESA Program).[7]

3. **Incentives Should be Whole Building, Performance-Based:** We were pleased to see the Scoping Report recognize the importance of "moving whole building multifamily programs from pilots to standard practice."[8] There are numerous examples of why prescriptive, unit-by-unit approaches such as those employed by the CPUC's ESA Program are inefficient and inappropriate when applied to retrofitting complex multifamily buildings. The complex utility systems of these larger buildings require that work be done at a whole building level if we hope to achieve the energy savings goals in the State's Long-Term Plan. Also, the ESA Program's insistence that contractors individually qualify every low income household even when certified income information is available at a property level is inefficient and a major barrier to reaching all units in these buildings.

4. **Low Income Incentives Should be Graduated Based on the Income Level and Number of Households Served:** Current state run-low income programs including the CPUC-regulated ESA Program and the CSD administered Weatherization Assistance Program (WAP) and Low Income Home Energy Assistance Program (LIHEAP) have a binary income eligibility system, meaning households either meet the single threshold level or do not qualify even if they are deemed low income under other state and federal programs. This is in contrast to state housing programs, such as the Multifamily Housing Program administered by the California Department of Housing and Community Development, which recognizes the need for differing levels of assistance for units serving households at a range of incomes (e.g. 30%, 50% and 60% of Area Median Income). We urge the CEC to rely upon the precedent of these HCD-administered programs to move the state towards a system of graduated incentives based on the relative depth of income served.

---

[7] California Public Utilities Commission, "Decision on IOU's 2012-2014 Energy Savings Assistance and California Alternative Rates for Energy Applications," Pg. 12.

[8] California Energy Commission Staff Report, "Comprehensive Energy Efficiency Program for Existing Buildings Scoping Report," Pg. 68.

5. **Income Eligibility Levels and Definitions Should be Standardized Across All State Low Income EE Retrofit Programs:** Unlike other low income energy programs administered by the U.S. Department Of Energy (DOE) and CSD, and contrary to standard practice in other federal and state programs, the CPUC's Policies and Procedures manual counts housing subsidies as income for the ESAP program. This difference is a major impediment to integrating the resources controlled by CSD and the CPUC and should be removed. The best solution would be moving ESAP and WAP to an AMI-based system. While there are challenges to converting the WAP program to County AMI from the current state AMI standard, it can be done at least partially through a conversion table used by HCD in setting MHP subsidy levels. Unlike WAP income eligibility standards which are in large part determined by DOE, ESAP eligibility levels are completely under the control of the CPUC and can and should be changed to an AMI system that can be better integrated with other programs that operate in California counties and recognize the importance of variations in income levels and construction costs across our state's diverse geography.[9]

6. **Owners Should Have a Role in Contractor Selection and Work:** The direct install approach traditionally relied upon by the state to provide low income energy efficiency services to all low income residential buildings is inappropriate for multifamily rental buildings for the following reasons: 1) owners are rightfully reluctant to allow contractors whose qualifications they have not reviewed to perform work of unknown scope on their properties; 2) the contracts used by direct install providers in the state's low income programs do not provide owners with industry standard assurances as to the quality of the work performed, the timing of work and communication with tenants, or their recourse in the event that there are problems [10]; 3) owners are generally not provided with inventories of the work performed and the appliances installed, which is a significant barrier to efficient maintenance of the buildings. For these reasons, we recommend the following: 1) wherever possible, owners should be allowed to choose their own contractor from lists of pre-qualified contractors; 2) contract templates should be developed that provide owners with industry standard rights and protections as well as basic rights for contractors; 3) even when there is a compelling reason why an owner cannot select it's own contractor, it is essential that owners have reasonable control over the timing, manner and location of work that is occurring and 4) that owners be given detailed inventories of all work done along with warranty information.

III. What Financing Tools Have Been Tried that Are Not Working?

1. **PACE[11]:** Property Assisted Clean Energy in which the cost of retrofits is repaid over time through voluntary special property tax assessments is a tool with tremendous power to finance energy retrofits in California but is generally not suitable to financing energy

---

[9] This week the California Tax Credit Allocation Committee, which administers the Low Income Housing Tax Credit program, announced their decision to use the RS Means construction index in recognition of the important impact that varied construction costs have on affordability statewide.

[10] In her testimony on October 8, 2012 at the CEC staff workshop panel on multifamily housing, Alicia Gaylord of Bridge Housing, relayed an incident where 700 light fixtures were installed through an incentive program, and subsequently all had to be removed due to poor workmanship.

[11] Referenced in the Scoping Report, pg. 102.

retrofits of multifamily rental properties because the lenders and investors will not accept adding costs to the property tax that are senior to their own liens.

2. **Property Secured Financing:** There have been several attempts to finance energy efficiency retrofits using traditional property secured loans. The most recent and comprehensive of these was the State Energy Program funded Bay Area Multifamily (BAM)[12] Fund undertaken by Enterprise Community Partners and the Low Income Investment Fund in conjunction with several Bay Area local governments. Initially, there was strong interest among owners in participating in BAM with more than fifty agreeing to conduct energy audits of their properties. In the end, however, only three (3) owners and six (6) properties agreed to participate. The main reasons for the low participation rate were: 1) owners could not justify spending the time of negotiating the permissions required from existing lien holders to add a relatively small amount of financing; and 2) owners were not willing to take on the risk of energy savings not materializing and being responsible for payments that would further strain their limited financial resources.

IV. What are the most promising solutions in development?

1. **Energy Performance Contracting** (EPC) in which a third party Energy Services Company (ESCO) takes responsibility for ensuring that a minimum level of savings is achieved and arranges for the financing of the retrofit, often through an Energy Services Agreement (ESA), has proven to be a very effective tool for a number of commercial building types. HUD specifically authorized Public Housing Authorities to enter into ESAs with ESCOs to retrofit older public housing. While a number of PHAs including San Francisco have taken advantage of this powerful tool, it's application to the multifamily sector has generally been limited to public housing where there is no split incentive problem because utility costs in public housing are generally paid for by and under the regulation of the U.S. government. Also, the ESCO/ESA model generally has only been shown to be cost effective for retrofits exceeding $1 million, which is far larger than the cost of the typical multifamily building retrofit. HUD has granted special permission for one program that is attempting to use the ESCO/ESA structure to retrofit 25 privately owned and managed low income properties in the eastern part of the U.S. Preliminary indications are that this effort has some promise for multifamily projects in California although there are questions about the cost effectiveness for individual multifamily properties as opposed to large portfolios such as the one being tested.

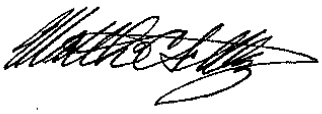
2. **On Bill Repayment (OBR) Financing:** OBR allows the cost of the energy retrofit to be repaid through a tariff placed on utility payments without any need for a lien on the property itself. Since OBR payments can be limited to an amount that is less than the estimated amount of the savings (Bill Neutrality), the properties can use the energy savings to finance the retrofit work. Three major advantages of OBR are: 1) no deed of trust is required, obviating the need to negotiate with senior lienholders as long as Bill Neutrality is observed; 2) private capital can be leveraged, stretching rate-payer and state funding; and 3) water savings can be combined with gas and electric savings. At the request of CHPC and other stakeholders, the CPUC recently ordered all of the state's Investor Owned Utilities to develop pilot OBR programs specifically for low income multifamily housing. The program design recommended to the

[12] Referenced in the Scoping Report, pg. 103.

CPUC by the IOUs' consulting team on October 2nd is based in large part on an early generation pilot OBR program that CHPC has developed working closely with SoCalGas in Southern California. Given the roughly 1:1 ratio of subsidy to the potential for private financing occurring at the first pilot site, we believe OBR has the potential to double the resources available to retrofitting low income rental housing properties in California. The current challenges facing OBR development include the need for 1) a loss reserve in the absence of comprehensive performance data on retrofit savings to provide assurance to private lenders that there is minimal risk to their capital; 2) matching low cost funds to bring down the cost of the 10-year OBR financing from the current estimated 7% interest to below 5% where it will be attractive to multifamily owners; and 3) assistance in paying for the comprehensive energy audits needed to estimate savings accurately and reliably.

Finally, I want to again thank the Commission for this opportunity to comment and inform the record on the importance of multifamily housing in reaching the goals of AB 758 and the California Long Term Energy Efficiency Strategic Plan. CHPC strongly believes the existing barriers to improving energy efficiency can be overcome, and we appreciate the innovative thinking evident in the Scoping Report. Please let me know if I can answer any questions or provide clarification on these comments. I hope you will consider CHPC a resource on multifamily issues moving forward.

Sincerely,



Matt Schwartz
President & CEO