

Turn facilities into high-performance assets





(and how to pay for it)

Ever have an idea for an improvement project at your facilities, but it gets derailed because your CFO doesn't want to fund the investment? Maybe the chiller is at the end of its life, the light fixtures haven't been upgraded to meet current standards, or the roof is aging and needs replacement or resealing. Tenants are changing over and it's time to spruce up the space, replacing windows and insulation, even switching to LED lights. These measures all come at an upfront cost, but not if you are savvy in how you finance them.

To both an owner and facility manager, it's in everyone's best interest to attract and retain high-value tenants with modern, high-efficiency buildings. To do so, you must be able to communicate not only the scope of work, but financing options necessary to achieve the vision. This article aims to highlight and compare the various financing mechanisms available to facility managers and property owners to achieve these updates while eliminating the upfront cost. The following table and descriptions outline the mechanisms, their ideal applications and comparative advantages, and is followed by take-away tips on how to articulate the financing component of your project vision to gain approval and bring your vision to fruition.

There are a lot of options, and within each there are numerous considerations for facilities managers to evaluate. There are some fundamental components of each mechanism, however, that can assist facility managers in the analytical process of assessing the most appropriate and cost effective one. Let's delve a bit deeper into each.

Having your options and investment benefits clearly articulated can make the difference between a tactical win, or being sent back to the drawing board.

FINANCING MECHANISM	C-PACE	CAPEX BUDGET	EQUIPMENT LEASE	ESCO	ON-BILL REPAYMENT
Upfront cost	None	Full amount	Varies	Varies, typically none	None (but generally not 100% of cost)
Term/duration of financing	10 to 30 years	N/A	5 to 7 years	EUL of measures	5 to 10 years
Primary credit for financing	Secured by property	N/A	Creditworthiness of Building Owner	Creditworthiness of Building Owner	Creditworthiness of Building Owner
Can financing reimburse owner for previous expenditures?	Yes	N/A	No	No	No
Tenants pay for share of financing payments?	Yes	No	Yes	No	Yes
Ideal applications	Efficiency, Solar, Water Conservation, Seismic and Storm Strengthening, Adaptive Reuse, Repositioning	All types of energy upgrades	Solar, and Mechanical property upgrades	Various	Efficiency upgrades

c-pace

Commercial Property Assessed Clean Energy, better known in the industry as C-PACE, is a relatively new financing mechanism gaining traction across the U.S. commercial real estate community. C-PACE is catalyzing improvement projects that enhance cash flows for property owners, with the potential to improve net operating income, reduce the cost of capital for building improvements, and attract and retain tenants by reducing the overall carbon footprint of properties while making them more comfortable. The key to C-PACE is that repayment happens through the owner's property tax bill over a long period of time, helping to keep payments low. C-PACE solves many problems which have historically prevented commercial property owners from implementing energy efficiency retrofits or environmentally-minded new construction projects, including:

UPFRONT COST. *Capital is often scarce for property upgrades and unfortunately, capital expenditures ("CapEx") for energy projects is typically at the bottom of the pile, leaving facility managers with few choices to fund their projects. With C-PACE, property owners receive 100 percent upfront financing (including soft costs) for qualified improvements.*

CREDITWORTHINESS. *C-PACE financing is based predominantly on the value of the property, not on the creditworthiness of the property owner, which eliminates the need for personal financials from the owner (and there are no personal guarantees!).*

INVESTMENT. *If a property is purchased and held for investment purposes, it can be hard to justify taking on additional indebtedness for projects that show an ROI longer than the hold period. C-PACE financing is non-accelerating, and is automatically transferred to the new owners upon the disposition of the property (although may be prepaid if desired).*

REIMBURSEMENT. *Some projects are time sensitive, such as roof replacements or a chiller in the summer. For property owners who do not have the luxury of waiting for outside capital before starting the project, C-PACE can be used to reimburse building owners for work that has already been completed, allowing them to replenish their capital reserves.*

DURATION. *One of the primary advantages of C-PACE are the long terms (up to 30 years), which enables repayment of an obligation over a longer period of time than traditional bank financing providing a lower annual payment and more flexibility.*

LIMITED COVERAGE. *C-PACE is not available everywhere. Though available in 34 states and the District of Columbia, be sure to consider whether your building falls within a jurisdiction that has C-PACE-enabling legislation. You can do so at [Clean Fund](#).*

How to sell your vision

As most facility managers know, capital spending and ROI are pivotal considerations when discussing any improvements with their leadership or property owner. Some facility managers are not well versed in framing the financial aspects of a project. And, it is always appropriate to seek out subject matter expertise when your own experience may be limited.

As the liaison between tenants and owners, you know the concerns and needs of all parties. To bridge those needs and keep everyone satisfied, here are some talking points to make that happen:

Sell the project on cash flow.

This is applicable for all financing mechanisms. Emphasis on the positive boost to NOI should get the attention and motivate property owners. In some cases, such as with C-PACE, new cash flows can be turned on (from solar, for example), even with no money out of pocket.

Sell it as a means of aligning owners and tenants.

The ability to share the repayment, regardless of financing mechanism, enables tenants to have a stake in the improvements they benefit from, while further reducing the owner's out of pocket cost (or cost of capital, depending on selection).

Sell it on Net Present Value ("NPV").

While C-PACE typically offers the highest NPV across financing mechanisms, communicating how and how much 'bang' property owners get for their buck now and over time is key in articulating the value.

Sell it as an expansion of available credit.

By financing a capital improvement project, ownership can retain cash and borrowing capacity for core business needs and more accretive investment (e.g., buying a building).

Hopefully, this has clarified the financing landscape and language in a way that helps engage the owners of the facility in conversation around the vision for improvements to both the facility and the NOI.

capex budget

CapEx Budgets are allocations of capital that companies set aside to pay for an upgrade and/or maintenance of physical assets. As with other options to pay for upgrades, there are positives and negatives to a company using their CapEx budget, and they vary widely depending on the company's long-term strategy for a particular asset. In a general sense, though, there are key items to note if you're considering using your company's CapEx budget:

SELF-SUFFICIENCY. *Using your company's CapEx budget is a self-sufficient approach to asset management. Among other benefits, financing projects with one's CapEx budget will make it easier to obtain financing by using your owned assets as collateral, and by not adding additional indebtedness to the balance sheet. The pitfall, of course, is the opportunity cost associated with not applying this (usually scarce) capital to other projects or investments. In other words, while it is nice to avoid taking on additional obligations, the CapEx budget capital put towards projects is unavailable for strategic uses across the ownership's investment and/or business.*

INTROSPECTIVE BY DESIGN. *The risk and discount factor on investment are inherently subjective, as they're up to the project manager and his/her team's perceptions. For this reason, it is hard to explicitly compare the utilization of CapEx and an investment return on a project to an average scenario for any of the other financing mechanisms covered here.*

equipment leases

Equipment Leases are a rental agreement for an asset from a lessor. Typical assets rented include various types of mechanical equipment with longer useful life spans. In contrast to capital leases, a third party will own the asset and retain the tax benefits associated with ownership.

CASH FLOW FLEXIBILITY. *Payments will be generally lower than options where asset is financed with a short-term loan. Purchase options allow for flexibility and optionality at the end of a lease.*

EFFICIENT USE OF TAX BENEFITS. *Ownership of the asset by a third party can result in lower payments due to efficient usage of the various depreciation and tax credit benefits of ownership. Generally, operating lease payments are booked as operating expenses, resulting in a reduced tax liability. Depending on the structuring of the operating lease, payments may impact property NOI.*

LIMITATIONS. *Because of limited security interest and the difficulty of repurposing collateral, many lessors will have high credit standards for approval or require some guarantee. Lessors may require or directly charge for insurance and other costs associated with equipment maintenance.*



esco

Energy Services Companies, or “ESCOs”, operate as energy efficiency consultancy experts, with the benefit of potentially offering an Energy Savings Performance Contract (ESPC) model, in which the ESCO utilizes the energy savings from a project to pay for the proposed upgrades. The ESCO will source, install and monitor the building efficiency upgrades, and the owner then uses the accrued savings to pay the ESCO for their services over time, the specific terms for which are outlined in the ESPC.

PROJECT RISK REDUCTION. *Because the ESCO is guaranteeing the project’s savings, and the building owner is paying for the upgrades through those accrued savings, the owner’s risk profile for the project is significantly reduced.*

ESCO EXPERTISE. *Related to the above, ESCOs are subject matter experts in what they do, which is energy efficiency upgrades. Their extensive design and implementation experience mitigates technical and performance risks, and can provide comfort to a building owner that they’re in good hands. As a facility manager, an ESCO needs you to best understand the needs and character of the facilities you oversee, but you, too, can benefit from the relationship as another expert voice advocating for the improvements.*

PROJECT LIMITATIONS. *Typically, ESCOs won’t work on projects for less than US\$1,000,000, as the costs associated with energy modeling for Measurement and Verification (“M&V”) makes the project unfeasible. As such, ESCOs usually focus on very large projects and typically with very high credit quality building owners or public sector projects.*

LONG PROJECT DEVELOPMENT CYCLES. *Working in facilities management, it likely comes as no surprise that projects can take what feels like forever to develop. ESCOs are, unfortunately, no exception to this fact, and because they’re guaranteeing the savings, they take significantly more time upfront in engineering cycles surrounding M&V. Long project development cycles are among the primary reasons that ESCO projects have a comparatively high drop-out rate.*

on-bill repayment

On-bill Repayment, or “OBR” options require the building owner to repay a project investment through a line item on their monthly utility bill, with the upfront capital being provided by a third party, not the utility (albeit, supported by utility rebates for energy reduction investments). The on-bill repayment allows for a streamlined approach because the utility has a pre-existing relationship with the end client who is billing them monthly for utility expenses.

CONVENIENCE. *Since the repayment mechanism is in place, facility managers may view this as an easy, convenient solution that doesn’t significantly interfere with their day-to-day.*

FLEXIBLE REPAYMENT. *In buildings with multiple tenants who are paying for property expenses such as taxes and utilities, facility managers have an opportunity to structure the repayment in such a way that everyone shares in the obligation. Furthermore, because the obligation is on the property’s utility bill, it can be passed through to tenants under many lease types. Note that, if transferability is not allowed, then businesses must pay off the entire loan upon sale of the property.*

LIMITED COVERAGE AREA. *OBR’s are not available everywhere, and before considering this option, you’ll need to verify that your utility allows this type of billing system before pursuing this approach.*

As a Senior Associate on the Business Development team, **Danny Robert’s** primary focus is on originating Commercial PACE projects, cultivating relationships with channel partners and commercial real estate owners, and screening, sizing and structuring CPACE transactions. He works closely with commercial property owners and managers to ensure the scope of work is clear and the process of financing runs smoothly for all stakeholders. Prior to joining CleanFund, Danny worked on the marketing team at NextGen Climate, and was a regional ambassador for the CleanTech Open, the world’s largest cleantech accelerator. Before moving to San Francisco in the fall of 2015, Danny spent 3 years in Tel Aviv growing a small software-as-a-service startup. He holds a B.S. in Business Administration from CU Boulder.