BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF CALIFORNIA

Order Instituting Rulemaking to Investigate and Design Clean Energy Financing Options for Electricity and Natural Gas Customers	Rulemaking 20-08-022

OPENING COMMENTS ON IOU AND PARTY CLEAN ENERGY FINANCING PROPOSALS of Gridium Inc.

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Gridium Inc. (Gridium) provides the following comments in response to the financing program proposals submitted by the IOUs and the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) program on June 15, 2022.

Gridium's focus as a business is on decarbonization of commercial buildings, enabled by our analytics software and by financing. Gridium is one of the largest On-Bill Financing (OBF) implementers in California. From our experience, finance programs are the key to cost-effective energy efficiency in large, privately-owned commercial buildings.

We focus our comments below on the CAEATFA program, which we find to be the most innovative, promising finance program among those submitted.

I. COMMENTS on CAEATFA proposal

We are supportive of the CAEATFA large business program as a whole. We believe large businesses should be supported in their efforts to decarbonize, as should other approaches to carbon reduction beyond energy efficiency. However we find issue in the fact that CAEATFA's Non-Residential/Large Commercial (NR/LC) financing program does not offer credit enhancement to large, privately-owned commercial buildings. The majority of our comments are devoted to this question.

Our understanding from discussions with CAEATFA staff is that CAEATFA has not proposed credit enhancement for its NR/LC program due to the Commission's ruling in D.13-09-044.[1] This ruling disallowed credit enhancement for medium and large customers.[2] The CPUC, with new facts at hand, has a chance to revisit this provision of D.13-09-044 and, in so doing, help the market for energy efficiency flourish.

The CPUC decided in D.13-09-044[3] that there should be no credit enhancement for medium and large businesses making use of On Bill Repayment (OBR) financing mechanisms. At the time of the issuance of D.13-09-044, the rationale of the CPUC was that "There are limited funds available during the pilot period, and no clear evidence of need for CEs [Credit Enhancements] by medium and large businesses."[4] The underlying facts have changed in the intervening 9 years, and the facts no longer support denying valuable credit support for PPP-paying medium and large customers. On this basis, we ask that the CPUC direct CAEATFA that credit enhancement should be used for medium and large customers in CAEATFA's NR/LC program.

Facts present in 2013 have changed

The following factual assertions upon which D.13-09-044 it is based are no longer true:

1) **Rationale that "There are limited funds available" is not, in a practical sense, true.** At the rate of credit support currently authorized by CPUC decisions, approximately [$700m] of projects could be performed in the next [five] years without exceeding the CAEATFA budget. And if these funds are exhausted in the future, this would be a good opportunity for the CPUC to allocate more funds to the rare successful energy efficiency program. In fact, only $2 million in loans have been issued thus far under the GoGreen

[1] CPUC Decision 13-09-044, issued Sept. 19, 2013.
[2] *Id.*, at 65.
[3] *Id.*
[4] *Id.*, at 65.

Business program. The danger is not overspending – the danger is another undersubscribed energy efficiency program.

In addition, according to CAEATFA documentation, half of the total loan amount issued thus far under the GoGreen Business program is for loans of $50,000 or less. Small loans, presumably for the smallest businesses, are not being crowded out.

2) **Rationale that "No clear evidence of need for CEs by medium and large businesses" has been rendered false by the COVID-19 pandemic.** The massive shift in working patterns due to COVID-19 has increased vacancy rates in commercial office buildings. This increase in vacancy rates has increased private financing institutions' perceptions of the risks inherent in supplying funds to projects in commercial office buildings. Gridium has had five projects in office buildings interested in the GoGreen program rejected at the underwriting stage because of financing institutions' concerns about the buildings' credit quality due to the COVID-19 pandemic.

Misconceptions surrounding the customer class that includes large buildings

Large commercial buildings are often large businesses. However, their financial structure is engineered to accomplish two things: first, pass through costs to tenants and second, insure the funds that own them from liability in the case of financial distress. These issues are the key to why efficiency work in large privately-owned commercial buildings has remained relatively limited. This is also the reason for the resounding success of PG&E's OBF program. The utility-provided credit support and bill pass through has made PG&E's OBF one of the largest, most successful efficiency programs in the state, limited mostly by budgets and by PUC-imposed TRC thresholds. The GoGreen Business program, with credit support and OBR, addresses both credit and pass-through issues as well, and we expect it to be many times the size of the OBF program.

Misconception 1: The large investors who own commercial buildings pay the energy bills

In the vast majority of commercial buildings, the tenants pay the energy bills. Utility costs are passed through to tenants by landlords, divided usually on a square foot pro-rata basis. This means that tenants benefit when bills are reduced. It also means that because landlords do not pay the bills, they are not incentivized to implement efficiency projects that lower those bills. OBR cures the split incentive, and allows tenants to benefit from lower energy bills in the long term.

Misconception 2: Only large investors benefit from energy efficiency

Large commercial buildings in fact serve small businesses. Employees of small businesses fill their hallways, their conference rooms, their desks. Small businesses pay their bills. Small businesses rent space because they cannot afford to own it. The tenants of multi-tenant commercial buildings in California are everyone from architecture firms to social service non-profits to yoga studios to tech startups to coffee shops to blood testing labs. These are the companies that pay the energy bills. These are the companies that, indirectly, pay into PPP funds for decades, and would benefit from the lower energy bills that efficiency projects provide. Any argument for equity around OBR credit support would include large office buildings because of the diverse small businesses they serve.

Misconception 3: large commercial buildings have access to vast pools of capital

While they are often owned by pension funds, insurance companies, REITs or major banks, large commercial buildings are entities with relatively small amounts of cash on their balance sheets. A building appraised at half a billion dollars may have cash on its balance sheet of a few million dollars, most of which is allotted to cover the next year's budget. Therefore, the LLCs that own the buildings themselves do not have the capital to do efficiency projects. This lack of cash and of credit is the reason it is so hard for the entities that own these buildings to participate in the Energy Savings Agreement (ESA) market that hospitals, municipalities and other credit-rated entities have made such good use of. It is also precisely the reason that OBR, with credit enhancement, promises to unlock the market for efficiency in large buildings. It's the same reason that the commercial solar industry has not reached its full potential – a lack of cash and credit in the entities that own buildings that would put up solar arrays on their roof and parking lots.

In addition, the entities that own these buildings cannot obtain capital from the parent funds. The structure of the parent funds is such that they do not provide capital to the buildings for projects – the finances of these funds are designed to be a one-way flow of capital.

Similarly, these buildings rarely have the ability to ask their mortgage lenders to re-open the mortgage to borrow for efficiency projects by providing a security interest in the building and/or land. This is one of the main reasons for the minuscule size of the Commercial Property-Assessed Clean Energy (PACE) market.

Misconception 4: lenders are eager to make unsecured loans to large buildings

This misconception stems in part from the low interest rates that commercial buildings enjoy on their mortgages. Financial institutions are eager to make loans to commercial buildings when these loans are secured by the property. However, when the loans are unsecured, or secured only by a UCC filing against building equipment that cannot effectively be removed, financial institutions are extremely reluctant to lend to commercial buildings.

Gridium has held conversations with about 20 financial institutions with the goal of having these institutions lend to large commercial buildings under the OBR program. We have successfully worked with one of the GoGreen program's lenders, Prime Capital, to enroll them in the program. We know the lender landscape better than most organizations, and have deep connections in the finance world through our experience in energy efficiency and solar.

Nevertheless, we have found lenders extremely reluctant to lend to efficiency projects in large commercial office buildings. Of the lenders currently enrolled in the program, three lenders have declined entirely, one lender has a limit of seven years, which is not enough for most projects, and another has loan limits that are too small for large commercial projects. We have found only one current program lender will engage in a serious way with large commercial office projects. The universal objection we hear from lenders is the lack of creditworthiness of large non-MUSH commercial buildings. The only cure for this objection, in our experience with lenders, is credit support.

Misconception 5: all large buildings are the same

Large buildings owned by public or creditworthy entities, often referred to as the MUSH (Municipal, University, School, Hospital) market are fundamentally different than buildings owned by private companies. First, MUSH buildings are almost always owner-occupied, so they do not suffer from the split incentive issues of privately-owned buildings. Second, MUSH buildings have access to the credit markets because of their status as creditworthy entities – and so have access to other sources of debt funding. Writ large, MUSH buildings do not need access to credit enhancement and have long enjoyed the services provided by energy services companies who serve them because of MUSH creditworthiness. Therefore MUSH buildings do not need the same ratepayer and public support as privately-owned buildings. We propose the two categories of buildings could be treated differently.

Opportunity with medium and large customers

Cure market failure

OBR with credit enhancement helps building owners and tenants overcome the split incentive and helps lenders overcome their reluctance to lend to non-creditworthy entities. The existing structure of the large office market is the existing structure – none of us participating in this proceeding can wish that way. Yet the CPUC has the opportunity here to cure the market failure created by that structure, and in so doing support a class of customers and their tenants who have diligently paid PPP funds for decades.

In curing this market failure, the risks taken by the CPUC with ratepayer funds are extremely low. The state's largest OBF program, at PG&E, has a 0.007% default rate.[5] We expect CAEATFA GoGreen Business programs to have a similarly low default rate. Yes, it's surprising that with such a low default rate lenders would ask for credit support – but nothing strikes fear in the heart of a banker like the prospect of having to explain to his or her credit committee why they made a bad, unsecured loan. As a reminder, if projects do not default and credit support is not used, the funds are returned to ratepayers. This makes credit support decidedly more cost efficient than classic incentive programs.

[5] *2021 Energy Efficiency Annual Report,* PG&E, at 47.

Enormous potential savings

If this market failure is cured, the CPUC will open up an enormous potential for energy efficiency. Thirty-seven percent of electricity use in California take place in commercial buildings.[6] And, in the United States, about 51% of commercial floor area is in buildings larger than 50,000 square feet.[7] This indicates large commercial buildings represent a significant portion of California energy use.

In a typical deep retrofit that Gridium performs in a commercial office building, we see a 15-25% energy reduction. Sometimes these reductions are greater, on the order of 30-40%. These reductions are achieved with non-heroic measures such as new controls, variable frequency drives and LED lighting. The key is not the technologies, but the on-bill financing itself. And, monitoring thousands commercial buildings with our energy management software, we see this opportunity in thousands of commercial buildings across the state.

Suggested CPUC actions re: CAEATFA

We suggest the CPUC take the following actions:

1) *Update guidance from the 2013 decision and allow for credit support for medium and large businesses.* There are two possible paths to this adjustment. One path would have CAEATFA revise its current GoGreen Business regulations[8] to explicitly allow medium and large businesses into the existing program. This would be straightforward and could be accomplished in a relatively short time frame. The other path would have CAEATFA establish a NR/LC program that was authorized in 2013, but do so with credit enhancement for medium and large businesses.

   We believe there is appetite for much more credit support than specified in currently regulations, but we also believe the regulatory and quality assurance (QA) and TRC

[6] California Energy Commission, *California Energy Consumption Database*

[7] U.S. Energy Information Administration, *Commercial Buildings Energy Consumption Survey, 2012*

[8] Cal. Code Regs. tit. 4, §§10092.1-10092.15

strings that would come attached to higher levels of funding would slow the program down so much as to drastically reduce its effectiveness.

We do not believe credit support is necessary for MUSH buildings for the reasons articulated above. We are agnostic as to which path is taken and believe CAEATFA should be left to decide based on efficiencies of program design and regulation.

II. Comments on PG&E Clean Energy Financing Options (CEFO) proposal

We find commendable PG&E's innovative, holistic proposal to address some of the constraints faced by OBF programs. In particular, we support the broad idea of building a platform that uses private, government and ratepayer funds efficiently. Ratepayers effectively pay for the credit rating of PG&E that will presumably backstop this program – this proposal helps ratepayers reap the decarbonization benefit of that ratepayer subsidy for PG&E's credit rating. The proposed structure will also benefit commercial customers, as they will have access to a well-run, well-funded program to improve their buildings' efficiency and lower their energy costs. We also support the inclusion of other behind-the-meter technologies, such as solar, in the PG&E proposal – the credit and split incentive issues that energy efficiency faces are also faced by these other decarbonization technologies.

The PG&E team is well aware that the most difficult part of this sort of plan is arranging for participation by private capital providers. We would like to know from PG&E more details about these discussions and about how the CPUC can support participation of private capital.

Suggested CPUC actions re: PG&E

1) *Approve PG&E's innovative plan*

   The Commission should approve PG&E's CEFO plan. It should also request more details on how CPUC policy can be aligned to smooth the entry of private capital into the OBF market.

2) *Consolidate all OBF programs under PG&E*

   PG&E has uniquely demonstrated its ability to foster programs where OBF can prosper. PG&E deploys nearly as much OBF funding *every year* ($70m) as SCE has across the entire 14 years of its OBF program life ($99m). As an alternative to having CAEATFA run all OBF/OBR programs, PG&E should administer all OBF programs in the state. Ratepayers and customers would gain from the efficiency and scale.

It is unclear to us why the CPUC allows the individual PAs to incur the expense of administering all these efficiency finance programs separately, with the PAs' varying degrees of enthusiasm and varying degrees of success. An efficiency project is an efficiency project whether it happens in Manteca or Bakersfield. Digital HVAC controls and LED lights are the same in either location. Multiple PAs also mean increased costs for implementers and, ultimately, customers – navigating the documentation requirements of multiple PAs is extremely costly.

3) *Follow CPUC's own guidance and revisit the TRC for OBF programs*

Of note, little of the work done on OBF to date will have impact on the state's decarbonization goals as long as TRC calculations continue to stymie OBF rollout. The CPUC should follow its own precedent[9] and revisit cost effectiveness tests for financed programs. If it does not, we risk looking back in five years and wondering why we spent all this time on this proceeding without fixing the TRC issue that is the primary hurdle for OBF program growth.

[9] D.09-09-047, *Decision Approving 2010 to 2012 Energy Efficiency Portfolios and Budgets,* September 24, 2009, at 288.

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Respectfully submitted,

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