OREGON SOLUTIONS

MEMORANDUM

TO: Lloyd Green District Project Team
FROM: Langdon Marsh
SUBJECT: Financing Options
DATE: April 3, 2009

BACKGROUND

One of the major purposes of this Oregon Solutions project is to outline financing options for projects and activities needed to achieve the goal of creating the most sustainable business district in the world. The governance entity or entities chosen will have some or all of the responsibility to provide or arrange financing for the selected projects and activities.

POTENTIAL FINANCING TOOLS IDENTIFIED IN THE PLAN

The *Lloyd Crossing Sustainable Urban Design Plan & Catalyst Project* (SUD Plan) includes as part of its discussion of a new organization to assist in meeting sustainability goals, the statement that, "A new entity is needed to facilitate the **financing**, construction, and maintenance of infrastructure and the implementation of sustainable development strategies and programs."

The Plan states that its vision can be achieved by utilizing a combination of existing tax credits, incentives and reinvestment of operational savings…."[1] It goes on to say that "Implementation of the vision will require strong public/private partnerships, patient capital and a long term perspective. Applying certain assumptions regarding the amount of operational savings and tax offsets assumed to be reinvested, these revenues alone are adequate to pay upfront capital costs over the 45 year study period; however, it will be important to identify additional public sources of capital to both make the required initial investments in infrastructure and to supplement the private capital sources identified in the Plan."[2]

According to the Plan, a Financial Model can display costs and revenue sources to reach a net cash flow projection that can be used to assess the financial performance of various strategies in 5 year increments. Adapting that model to the current circumstances would allow various sustainable strategies to be assessed to determine the net cash flow requirements over time. The Plan projects the need for significant public capital to provide upfront capital costs and to cover shortfalls in revenue until the projected savings from sustainable infrastructure investments begin to break even over 30-40 years.

[1] SUD Plan, p. 13.
[2] Id.

Among the existing funding sources identified in the Plan are:

1. Urban renewal tax increment funds generated from within the urban renewal district that covers the Lloyd District. (PDC could provide information on how much time and bonding capacity is left in the District).
2. Operational savings, from water and energy investments
3. Local improvement district financing (LID)[3]
4. Federal and State tax incentives (for energy strategies)

The Plan identified some potential new sources:

1. earmarking a portion of System Development Charges, on the theory that the improvements in Lloyd would take the area largely off the City's infrastructure grid
2. reallocating portions of Bureau of Environmental Services capital budget, because the improvements would reduce the size of infrastructure improvements needed and improve environmental conditions
3. New Market Tax Credits, for investors in disadvantaged communities including urban renewal areas. This program has just been reauthorized as part of the Federal Stimulus Package.

The Plan also listed some potential regulatory incentives, capital subsidies and private contributions:

1. Reduced private open space requirement
2. Transferable development rights
3. Corporate sponsorships
4. Transfer open space from outside the district, like a mitigation bank
5. City matching program to leverage private foundation funds
6. Construct public parking garage and allocate some of the spaces to meet developer requirements, with developers investing savings in district improvements
7. Partnerships with large property owners, to create co-funded programs with integrated results
8. Parking lot redevelopment, with a subsidy to create underground parking spaces with surface parks; the City portion of revenue could be dedicated to park O & M

The Plan does not discuss these in detail, nor analyze the practical and political feasibility of implementing them. It is a useful list, however, of some potential sources that might be pursued, depending on the kinds of projects chosen and the need for and timing of financing or incentives.

[3] House Bill 2181 is now in the Oregon Legislature. It would authorize local governments to establish local improvement district within which owners of qualifying residential and commercial property may receive loan financing of energy efficiency and renewable energy improvements to property. It also authorizes the State Department of Energy to make loans to finance energy efficiency improvements to existing real property in districts.

NEED FOR PUBLIC FINANCE, SUBSIDY OR INCENTIVE

A threshold question is whether and to what extent participants in the District will need some form of public subsidy in the form of financial incentives, low interest loans, tax credits or grants. Before looking for subsidy for a particular improvement or set some kind of need analysis should be done, along the following lines:

1. **Short payback**. Some of the improvements, individual or joint, may have sufficiently large avoided costs or short payback periods that participants would be willing to make them without any subsidy. This might be true, for example, for some of the landscape, garden and habitat improvements and rain or stormwater absorption areas, or for energy efficient windows or lighting.

2. **Increases in value**. Other investments might have such direct impact on the value of the benefiting properties that no subsidies or incentives are needed. Private market rate financing would be sufficient. Innovative design features that had both resource efficiency (light, water, energy) and created amenities for occupants or the public that attracted traffic to the businesses in the area might fall into this category.

3. **Non-monetary incentives**. Short of direct public subsidies, regulatory or privately agreed upon incentives are another means of inducing investment. The Plan lists some of the available ones. EPA's Smart Growth program has identified over 200 that could be considered for this project. Analysis of existing or new governmental or privately agreed incentives should be done for the actions and investments selected by the Lloyd District Solutions Team. The City, Metro or the State might be willing to provide additional targeted incentives.

4. **Externality markets**. Some investments will create currently unaccounted for benefits that can be measured, monetized and sold into existing or future markets, offsetting the additional costs involved. The entity created for the District could serve as an aggregator of these benefits and trade or sell them on behalf of the District, using the proceeds to help pay the improvement and maintenance costs. Many of the improvements will, for example, create real and measurable reductions in carbon emissions, which might not be worth the time and effort of individual property owners to measure, certify and market in the current voluntary, likely soon to be mandatory, carbon market. But the new entity could do it routinely. Another possible example is the ecosystem services from better water management, reduced runoff, improved habitat and mitigation of impacts from development. These might be sold in the emerging Willamette Valley Ecosystem Services Market. Future markets in other beneficial outcomes like pollution reduction of various kinds, mobility, health and security improvements, and even job creation and retention may be developed over the coming years to address externalities not currently accounted for by current markets, command and control regulation or public programs. Portland State University is

contemplating a center to explore these possibilities and Lloyd and the other Portland EcoDistricts would obviously be likely candidates for introducing new market or payment opportunities.

PUBLIC FINANCE AND SUBSIDY OPTIONS

To the extent that early paybacks, increased property values, incentives and existing or predictably available externality markets are not sufficient to induce the kinds of investments necessary to meet the Lloyd Green District objectives, the delta must be either financed by debt or subsidized by grants or other means, or both.

1. Debt Financing. There are a wide variety of tools available, depending on whether the investment is private or public in nature. There are also mixed instruments, like industrial development revenue bonds, which fund private investments that have public benefits. Many of the members of the Solutions Team are highly sophisticated and knowledgeable about the availability of these tools and the factors that lead to choices among them, so there is no need to start looking at them until the investments needing to be financed are identified. If the Team wants to know more about any of these tools, PDC or other members would be able to bring the best local experts to the table.

There are two potential ways to spread out the costs of financing that are worth raising at this point:

Longer finance terms. One way to reduce the burden of private or public financing would be to adjust the annual costs of debt service over the full term of the benefits that are expected, so that debt service payments do no exceed the periodic realization of those benefits. A typical 30 year loan with levelized debt service would not accomplish this, but a 40, 50 or longer year loan with lower initial debt service payments might be able to allow loan repayments to be in synch with the timing of the realization of the benefits. Another advantage is that debt service payments in later years would be made with inflated dollars. Most debt instruments are by practice or law limited to 30 or 40 years, generally the outer limit of the useful life of most investments. In the nineteenth and early twentieth centuries, it was sometimes the practice in the US and Britain to issue 100 year or even longer term bonds to finance long lasting infrastructure like railroads, canals and such. Analyzing the benefits and downsides of long term bonds for some of the permanent or very long lasting investments could be a very useful exercise once the desirability of these investments have been identified.
The feasibility of very long term bonds or low initial debt service instruments will depend on finding a willing issuer or lender, which has or can obtain the legal authority to provide this “patient capital”. It would be advisable to engage the Department of Energy and the State Treasurer in this conversation, both in terms of the State’s own energy, environmental and other public purpose loan programs and the State’s pension funds. A pension fund would be an ideal lender because it would have policy and

financial interest in investing in local projects that can return long term, steady income while benefiting the state and the pensioners in other ways.

Environmental District Bonds. While PDC and the State Energy Department are probably the most logical low interest lenders for projects, the City may also be able to play a role. There is a new district bonding concept that can finance a variety of local energy efficiency, renewable energy, air quality and non-point source pollution reduction projects. A recent example of such a bond has been in the City of Berkeley, which installed solar panels on willing residents' homes, paying for them with a twenty-year bond, and is paying off the bond through a special assessment on the homeowners who agreed to join the program. No referendum was required because only those who agreed to be in the program were assessed. Recent legislation authorizes other California cities to do the same. Similar efforts are underway in Colorado, Massachusetts and Annapolis, MD. In addition to solar panels, this voluntary bonding concept could finance energy efficient insulation, doors and windows, geothermal loops, green roofs, rain gardens, permeable pavement, and more—in fact any type of device that can be linked to real property by a lien. The lien guarantees that the local bond will get a low interest rate because of the inherent security it provides. The other favorable feature is that the term of payment can be far beyond what the individual property owner could get from a private lender. HB 2181, introduced this year, and a variety of other bonding mechanisms now available in Oregon to local governments, could potentially accomplish the same thing as the Berkeley example.

2. Subsidies. The number of subsidies available for many of the potential projects is large and growing and for the most part are well known to the members of the Solutions Team. They range from State grants and subsidized loans from the Departments of Energy, Environmental Quality, Transportation and probably others to Federal grants from a variety of Agencies, including DOE, EPA, DOT and DOA. Rather than try to list them now, it would make sense to investigate them in the context of what the Team is most interested in pursuing. There are private experts in grant getting that might be employed but I suspect there is sufficient expertise at the City and State level.

QUESTIONS FOR THE TEAM

1. What issues is the Team interested in hearing more about?
2. How much work should be invested before the May meeting to explore these or other issues?
3. What experts would the Team like to hear from at the meeting or sooner/later?