ENERGY STAR®
Money for Your Energy Upgrades

An Introduction to Financing Energy Efficiency Upgrades in the Public Sector
Today’s Discussion

- Paying for Energy Efficiency with Operating Budget Dollars
- Tax Exempt Lease-Purchase Agreements – the basics
- Performance Contracts – the basics
- Delaying the installation is an expensive decision
Public Sector Defined

- Governments
  - State
  - County
  - Local/Municipal
  - Agencies

- Schools
  - K-12

- Higher Education
  - State Universities and Community Colleges
  - Private Colleges and Universities
Private vs. Public Sector

- Approval Process
- Financial Instruments
- Authorization to Commit
Private vs. Public Sector

- Budget Savings
- Maintenance Savings
- Environmental Improvements
Goals of Presentation:

– Change traditional thinking about energy financing in the public sector

– Accelerate the installation of energy-efficient equipment
Energy Optimization

– Focuses on decreasing energy cost while increasing productivity

– Combines energy efficiency equipment with operational procedures that can transform energy bills into “cash flow opportunities”
These guidelines are the result of the “best practices” from top ENERGY STAR partners.

Put their expertise to work for your organization!
“We are paying for energy efficiency projects \textit{whether or not} we do the projects!”
So...

where does the money come from to pay for energy efficiency projects?
Capital Budget (Debt)
• What is the approval process?
  – Board/Council
  – Referendum
• Ceiling on capital expenses?
• Restructure capital expense budget?

Operating Budget (Expense)
• Already in utility payments
• Easier approval process
• Energy efficiency projects may provide access to captive funds for other needs
Categorizing Financial Instruments

• **Capital Expense**
  – Bonds
    • GO
    • Revenue
  – Loans
  – “Performance Contract”

• **Operating Expense**
  – *Lease/Lease-Purchase*
  – “Performance Contract”

• **No Expense**
  • Grants
  • Rebates/Incentives
Categorizing Financial Instruments

- **Capital Expense**
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Performance Contracts
Performance Contracting

Market segment trends over time for ESCO projects

Source: National Association of Energy Service Companies
“An ESCO, or Energy Service Company, is a business that develops, installs, and finances projects designed to improve the energy efficiency and maintenance costs for facilities over a seven to 10 year time period. ESCOs generally act as project developers for a wide range of tasks and assume the technical and performance risk associated with the project.”

www.naesco.org
What Services Can An ESCo Provide?

- Walk-through energy audit
- Comprehensive energy audit
- Design and specification of new equipment
- Vendor of energy efficiency equipment
- Installation/construction management
- Performance guarantees
- Ongoing maintenance
- Training of personnel
- Measurement and verification of project performance
- Financing
- Indoor Air Quality problems
- Procurement and purchase of energy commodity
What Services Can An ESCo Provide?

- Walk-through energy audit
- **Comprehensive energy audit**
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- **Ongoing maintenance**

- Training of personnel
- Measurement and verification of project performance
- Financing
- Indoor Air Quality problems
- Procurement and purchase of energy commodity
Common Performance Contracts

- Shared Savings Agreement
  - Fixed payment
    - One-time verification
    - Taxable or tax-exempt
  - Variable payment
    - Requires measuring and monitoring
    - More expensive
Common Performance Contracts

- **Guaranteed Savings Agreement**
  - Can separate financing from technical performance
  - Most commonly used for Public Sector

- **Own-Operate**
  - ESCo owns facility and sells back “output”

- “Chauffage”
  - Buy end-result, i.e., lumens or ambient temperature
Common Performance Contracts

Related but Independent Documents

– Project Development Agreement
– Energy Services Agreement
– Finance Agreement
Private Sector Financing
Why Companies Ask for “Off Balance Sheet Financing”?

• No Capital Budget for Energy Project
  – Freeze on Capital Spending
  – Competing with Other Projects

• Pay for Project from Operating Expenses
  – Cumbersome Capital Budget Process

• Restrictions on New Debt
  – Internal Restrictions
  – Over-leveraged
  – Covenants with Existing Lenders
What Qualifies as “Off Balance Sheet Financing”?

- Operating Leases
- True Performance Contracts
- Rental Agreements
- “Project Financings”
  – Large Projects
Tax-Exempt Lease-Purchase Agreements
(AKA Municipal Leases)
Benefits of Tax-Exempt Lease-Purchase Agreements

- **Title** to the Equipment Rests with Lessee
- Access to Low Cost, **Tax-Exempt Funds**
- Payments may be Subject to **Annual Appropriation of Funds** by Lessee
- Accommodates **Construction Financing**
- Payments *in arrears*
- You may already be leasing something!

**Fast and Easy!!!**
Tax-Exempt Lease-Purchase

- Three Considerations
  - **Legal**
    - Authority
    - Voter Approval Issues
  - Financial Reporting
    - GAAP/GASB
  - Internal Accounting
    - “Materiality”
When Is 5% Not 5%?

- **Bond**: Plus Fees
- **Lease**: Fees Included
An Incomplete Listing
(for illustrative purposes only)
Quantifying the cost of Delay
Energy Efficiency:
A Cash Flow Opportunity

ENERGY STAR® CASH FLOW OPPORTUNITY Calculator from the US Environmental Protection Agency.

This spreadsheet is designed to work with Microsoft Excel 97 or later versions. It may not work properly with earlier versions. It is best viewed with 1024x768 pixels resolution.

Version 1.1

Please send any comments to Melissa Payne, ENERGY STAR National Manager, at payne.melissa@epa.gov.
A simplified general approach

<table>
<thead>
<tr>
<th>Name</th>
<th>Example organization with multiple facilities adding up to 1 million SF</th>
</tr>
</thead>
<tbody>
<tr>
<td>Select Scenario</td>
<td>First Approximation</td>
</tr>
<tr>
<td>Sample Values</td>
<td>Sample Values</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>SF</th>
<th>Annual Energy Costs ($) - All Fuel Types</th>
<th>Savings Target (%)</th>
<th>Potential Annual Savings</th>
</tr>
</thead>
<tbody>
<tr>
<td>Group A</td>
<td>200,000</td>
<td>100,000</td>
<td>0.50</td>
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<tr>
<td>Group B</td>
<td>800,000</td>
<td>900,000</td>
<td>1.13</td>
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</table>

<table>
<thead>
<tr>
<th>Total SF</th>
<th>Total Energy Cost ($) - All Fuel Types</th>
<th>Weighted Savings Target (%)</th>
<th>Total Potential Annual Savings ($)</th>
</tr>
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<tbody>
<tr>
<td>1,000,000</td>
<td>1,000,000</td>
<td>1.00</td>
<td>28.50%</td>
</tr>
</tbody>
</table>

*Use existing data*

**Energy STAR**® does not guarantee that your project will generate the results presented herein. An investment grade audit performed by a qualified engineering organization is required to determine the actual size of your savings opportunity.
## The Value of Your Investment

**FIRST APPROXIMATION INVESTMENT OPPORTUNITY**

<table>
<thead>
<tr>
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<th>Group A</th>
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</tr>
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<tbody>
<tr>
<td>Annual Utility Bills</td>
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<td>$1,000,000</td>
</tr>
<tr>
<td>Annual Potential Savings</td>
<td>$15,000</td>
<td>$270,000</td>
<td>$285,000</td>
</tr>
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</table>

Potential Annual Savings = Cash Flow Opportunity

### What Can This Annual Cash Flow Buy?

- **Assuming an interest rate of** 5.00%
- **Assuming a term of** 7 Year(s)
- **Savings used to pay energy investments** 90%

**Taken from operating funds, these savings could finance energy projects equal to:**

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<th>Contribution that your operating budget can make towards energy improvements</th>
<th>/SF</th>
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<td>Simple Payback</td>
<td>Year(s)</td>
</tr>
<tr>
<td></td>
<td>Month(s)</td>
</tr>
</tbody>
</table>

Median project investment ranges between $1 - 3/ft².

- Consider blending short- and long-term projects to maximize use of the savings.

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*Market Trends in the U.S. ESCO Industry: Results from the NAESCO Database Project (http://www.naesco.org/ESCO_Mkt_Trends_final.pdf), May 2002*
## The Value of Your Investment

### First Approximation Investment Opportunity

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Potential Annual Savings = Cash Flow Opportunity

### What Can This Annual Cash Flow Buy?

- Assuming an interest rate of 5.00%
- Assuming a term of 7 Year(s)
- Savings used to pay energy investments 90%

Taken from operating funds, these savings could finance energy projects equal to: $1,512,000

Contribution that your operating budget can make towards energy improvements: $1.51/SF

Simple Payback: 5 Year(s) 4 Month(s)


**Important Notice**
Cash Flow

**FIRST APPROXIMATION CASH FLOW OPPORTUNITY**

Click this button if you would like to transfer values from Investment Values page. Year(s) postponed is given as 2 years.

<table>
<thead>
<tr>
<th>Project cost</th>
<th>1,512,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Simple payback</td>
<td>5 years</td>
</tr>
<tr>
<td>Interest rate</td>
<td>5.00%</td>
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<tr>
<td>Financing term</td>
<td>7 years</td>
</tr>
<tr>
<td>Year(s) postponed</td>
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</table>

**Cumulative Cash Flow Impact Comparison**

- **Option A (Fast Track Financing)**
  - **Option B (Waiting for Cash)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Savings</th>
<th>Cost</th>
<th>Annual Cash Flow</th>
<th>Cumulative Cash Flow</th>
<th>Savings</th>
<th>Cost</th>
<th>Annual Cash Flow</th>
<th>Cumulative Cash Flow</th>
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<tr>
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<td>($256,446)</td>
<td>$28,554</td>
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<td>$285,000</td>
<td>$1,339,888</td>
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<tr>
<td>11</td>
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<td>$0</td>
<td>$285,000</td>
<td>$1,624,888</td>
<td>$285,000</td>
<td>$0</td>
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</tr>
</tbody>
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**Net Present Value of Option A** $1,042,136  
**Net Present Value of Option B** $883,170

For purposes of this calculation, all cash flows are being discounted at the interest rate indicated in cell G7 - financing paid monthly in arrears.
# Cash Flow

## First Approximation Cash Flow Opportunity

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<tr>
<td>1</td>
<td>$285,000</td>
<td>$(256,446)</td>
</tr>
<tr>
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<td>$285,000</td>
<td>$(256,446)</td>
</tr>
<tr>
<td>3</td>
<td>$285,000</td>
<td>$(256,446)</td>
</tr>
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**Net Present Value of Option A** $1,042,136  
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For purposes of this calculation, all cash flows are being discounted at the interest rate indicated in cell G7 - financing paid monthly in 12 years.
# Cost of Delay

## First Approximation Cost of Delay

<table>
<thead>
<tr>
<th>Comparative Interest Rate Analysis</th>
<th>Use Cash Flow Values</th>
<th>Month</th>
<th>Balance at beginning of month</th>
<th>Amount lost in monthly utility bills</th>
<th>Balance at end of month</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate of immediate financing</td>
<td>5.00%</td>
<td>1</td>
<td>$51,400</td>
<td>$23,800</td>
<td>$27,700</td>
</tr>
<tr>
<td>Interest rate of a lower financing</td>
<td>4.00%</td>
<td>2</td>
<td>$27,700</td>
<td>$23,800</td>
<td>$3,300</td>
</tr>
<tr>
<td>Cost of the equipment</td>
<td>$1,512,000</td>
<td>3</td>
<td>$3,900</td>
<td>$23,800</td>
<td>($19,900)</td>
</tr>
<tr>
<td>Simple payback</td>
<td>5 year(s)</td>
<td>4</td>
<td>($19,800)</td>
<td>$23,800</td>
<td>($43,600)</td>
</tr>
<tr>
<td>Potential annual savings</td>
<td>$285,000</td>
<td>5</td>
<td>($43,600)</td>
<td>$23,800</td>
<td>($67,300)</td>
</tr>
<tr>
<td>Term of financing</td>
<td>7 year(s)</td>
<td>6</td>
<td>($67,300)</td>
<td>$23,800</td>
<td>($91,100)</td>
</tr>
<tr>
<td>Lower interest rate savings</td>
<td>$51,400</td>
<td>7</td>
<td>($91,100)</td>
<td>$23,800</td>
<td>($114,800)</td>
</tr>
<tr>
<td>Amount lost in utility bills</td>
<td>$23,800</td>
<td>8</td>
<td>($114,800)</td>
<td>$23,800</td>
<td>($138,600)</td>
</tr>
<tr>
<td><strong>Break-Even Point</strong></td>
<td></td>
<td>9</td>
<td>($138,600)</td>
<td>$23,800</td>
<td>($162,300)</td>
</tr>
<tr>
<td>Opportunity cost if delayed 12 months*</td>
<td>15.4%</td>
<td>10</td>
<td>($162,300)</td>
<td>$23,800</td>
<td>($186,100)</td>
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<td></td>
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<td>($186,100)</td>
<td>$23,800</td>
<td>($209,800)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>12</td>
<td>($209,800)</td>
<td>$23,800</td>
<td>($233,600)</td>
</tr>
</tbody>
</table>

*The opportunity cost is 12 months of lost savings divided by the original project cost.

To see values from the Cash Flow worksheet, click the Use Cash Flow Values button above. To close the spreadsheet, click the Save & Exit button on the CFO Calculator toolbar.

Important Notice
# First Approximation Cost of Delay

## Comparative Interest Rate Analysis

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**Important Notice**
**Cost of Delay**

**FIRST APPROXIMATION COST OF DELAY**

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<td>$3,900</td>
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<td>3</td>
<td>$3,900</td>
<td>$23,800</td>
<td>($19,900)</td>
</tr>
<tr>
<td>Simple payback</td>
<td>5 years (5 year(s))</td>
<td>4</td>
<td>($19,800)</td>
<td>$23,800</td>
<td>($43,600)</td>
</tr>
<tr>
<td>Potential annual savings</td>
<td>$285,000</td>
<td>5</td>
<td>($43,600)</td>
<td>$23,800</td>
<td>($67,300)</td>
</tr>
<tr>
<td>Term of financing</td>
<td>7 years (7 year(s))</td>
<td>6</td>
<td>($87,300)</td>
<td>$23,800</td>
<td>($91,100)</td>
</tr>
<tr>
<td>Lower interest rate savings</td>
<td>$51,400</td>
<td>7</td>
<td>($91,100)</td>
<td>$23,800</td>
<td>($114,800)</td>
</tr>
<tr>
<td>Amount lost in utility bills</td>
<td>$23,800</td>
<td>8</td>
<td>($114,800)</td>
<td>$23,800</td>
<td>($138,600)</td>
</tr>
<tr>
<td>Break-Even Point</td>
<td>2.2 months (2.2 month(s))</td>
<td>9</td>
<td>($138,600)</td>
<td>$23,800</td>
<td>($162,300)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>10</td>
<td>($162,300)</td>
<td>$23,800</td>
<td>($186,100)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>11</td>
<td>($186,100)</td>
<td>$23,800</td>
<td>($209,800)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>12</td>
<td>($209,800)</td>
<td>$23,800</td>
<td>($233,600)</td>
</tr>
</tbody>
</table>

*The opportunity cost is 12 months of lost savings divided by the original project cost.

Opportunity Cost if delayed 12 months* 15.4%

To see values from the Cash Flow worksheet, click the Use Cash Flow Values button above. To close the spreadsheet, click the Save & Exit button on the CFO Calculator toolbar.
Reminder

An investment grade audit done by a qualified engineering company will be required to determine the actual size of your opportunity.
How ENERGY STAR Can Help

• Peer Information
  • Similar situations that met with success
  • Impact of sharing the benefits
• Expert support with your financing process
• Assist with presentations to decisionmakers
Internet Presentations

Distance Learning Opportunities

- ENERGY STAR -Overview for Public Sector Organizations
- Higher Education ENERGY STAR Overview
- ENERGY STAR Overview for Service & Product Providers
- Benchmarking with ES Portfolio Manager
- Money for Your Energy Upgrades
- Introduction to The CFO Calculator
- Purchasing and Procurement
- PC Power Management
- Designing Top Energy Performing Building for Your Clients

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www.energystar.gov
Summary

- Significant cost savings are possible from energy efficiency projects
- Many projects are delayed or prevented due to financial concerns
- Third-party financing can provide funds for these projects
- Delaying projects is expensive
- ENERGY STAR can help identify third party financing that works for you
For More Information...

- **Neil Zobler**  (203) 790-4177  
  (Catalyst Financial Group, Inc.)

- Catalyst Financial Group, Inc. is an EPA contractor working for ENERGY STAR

- E-mail nzobler@catalyst-financial.com

- Call the ENERGY STAR Hotline at 1-888-STAR-YES (1-888-782-7937)

- Visit www.energystar.gov