

Date: February 14, 2019

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From: Brad R. Fletcher, Vice President

Subject: ***Resolution Authorizing Various Matters Relating to Bond Financing for Commercial Property Assessed Clean Energy Projects including Approval of Updates to the Authority's Bond Handbook, Fee Schedule, and Other Matters Related Thereto***

Request:

The accompanying Resolution requests approval of an updated Bond Handbook and Fee Schedule in connection with the Illinois Finance Authority's (the "Authority") commencement of offering Commercial Property Assessed Clean Energy ("C-PACE") bond financing services, and delegates authorization to Authorized Officers (as defined therein) to perform certain actions within established parameters.

Previously, on February 15, 2018, Members of the Authority adopted a Resolution conveying to the Executive Director and staff its support to develop financing options in response to failed implementation of state legislation enacted into law for local units of government on August 11, 2017.

Impact:

The Authority's launch of C-PACE bond financing services offers borrowers, local units of government, program administrators, and capital providers (or bond purchasers) a turnkey solution for standardized, efficient, and affordable bond issuance. Local units of government assign assessment contracts originated by capital providers to the Authority in order to utilize standardized bond documents and effectively pool assessment contracts across multiple jurisdictions in a program administrator's market area to achieve economies of scale. The Authority's C-PACE bond financing services promote standardization of an otherwise fractured Illinois C-PACE market to improve liquidity and bring about cost savings for all. The Authority has been granted \$2.0 billion of bonding authorization by the Illinois General Assembly to finance or refinance "PACE Projects" as defined in the Illinois Finance Authority Act (20 ILCS 3501/801-1 et seq.), which are "energy projects" as defined in the Property Assessed Clean Energy Act (50 ILCS 501/ et seq.) (collectively, "Energy Projects" herein). This \$2.0 billion of bonding authorization for Energy Projects is separate and apart from the Authority's general \$28.15 billion debt limit.

In furtherance of achieving economies of scale, private warehouse lenders can interim fund small Energy Projects that are otherwise uneconomical for purposes of long-term bond financing for up to three years. Small Energy Projects can therefore receive immediate funding to expedite construction and installation.

Upon a critical mass of assessment contracts being originated by a capital provider for small Energy Projects, the Authority, as a statewide body politic and corporate, can issue a pooled bond to the applicable capital provider, prorating the costs of issuance amongst the various borrowers in a program administrator's market area.

Background:

Pursuant to an enabling state statute, commercial property owners in Illinois can finance or refinance up to 100% of their energy efficiency, renewable energy, and water conservation projects on a long-term basis through a local unit of government that has established a PACE area within its jurisdictional boundaries.

Upon establishment of a PACE area by the adoption of a local unit of government ordinance, a commercial property owner can voluntarily enter into an assessment contract with that local unit of government to finance a qualifying Energy Project on the commercial property. Proceeds of a municipal bond issue by the local unit of government fund the Energy Project, and bonds are repaid through an assessment imposed by the local unit of government on the commercial property. The assessment contract constitutes a lien against the commercial property on which the assessment is imposed until the assessment, including any interest or penalty, is paid in full. The lien is recorded with the county and becomes a line-item on the property owner's real estate (i.e., property) tax bill. Like any other property tax, the lien is senior to any outstanding commercial mortgage. Accordingly, mortgage holder consent is required.

Bond repayment obligations financed through this voluntary assessment seamlessly transfer to any new owner upon sale of the commercial property. Similarly, the new owner of the respective commercial property continues to benefit from the ongoing savings from the energy efficiency, renewable energy, and water conservation project.

Importantly, bondholders are entitled to the same rights and remedies that a local unit of government has regarding delinquent property taxes. Cumulatively, these factors allow C-PACE bond financing terms to exceed standard commercial lending terms that are otherwise only 5-7 years, and as a result, C-PACE bond financing terms are more aligned with the useful life of Energy Projects. The useful life of Energy Projects can extend to 20 and even 30 years, depending on the Energy Project.

Finally, unless issued for a qualifying project under federal law (which are likely going to be in the minority of C-PACE bond financings), bonds issued for Energy Projects are not entitled to a tax-exempt interest rate benefit, unlike the vast majority of private activity bonds issued by the Authority.

Transformation Initiative:

On November 2, 2017, federal tax legislation was introduced in the United States House of Representatives that threatened to eliminate issuance of private activity bonds, the primary service by which the Authority generates income. Ultimately, however, Congress chose to eliminate advance refundings and mostly preserved the Authority's capacity to issue private activity bonds.

In response, the Authority undertook an effort to diversify its products and services (the "Transformation Initiative") while continuing to fulfill its public mission. The Transformation Initiative is based upon guiding principles established by the Authority's 2013-2015 Strategic Plan.

Initiating C-PACE Bond financing services was a cornerstone of the Transformation Initiative.

Legislative History:

I. Enabling State Statute

On August 11, 2017, the Governor signed into law HB2831 (Public Act 100-0077) cited as the Property Assessed Clean Energy Act. The law enables Illinois local units of government, including counties, cities, and villages, to establish property assessed clean energy programs within their respective jurisdictional boundaries.

Pursuant to the enabling state statute, a record owner of commercial property within a PACE area may enter into an assessment contract with a local unit of government to finance or refinance one or more qualifying Energy Projects. Eligible property includes privately-owned commercial, industrial, non-residential agricultural, or multi-family (of 5 or more units) real property, but does not include property owned by the local unit of government or a homeowner's or condominium association. Furthermore, the statute does not enable residential property assessed clean energy ("R-PACE") programs.

Unfortunately, no local unit of government created a commercial property assessed clean energy program within the first six months following enactment of the law. As a result, the Authority adopted a Resolution on February 15, 2018, conveying to the Executive Director and staff its support to develop statewide, centralized financing options for Illinois local units of government that desire to establish commercial property assessed clean energy programs in their communities. Implementation of this policy by the Authority required changes to the enabling state statute.

II. SB43 – IFA Act Amendment

On April 13, 2018, an amendment to the Illinois Finance Authority Act was filed in the Illinois Senate. After receiving recommendation by the Senate Commerce and Economic Development Committee, the Senate unanimously passed SB43 on its third reading April 24, 2018. SB43 arrived in the Illinois House of Representatives that same day. After receiving recommendation by House Revenue and Finance Committee, the Illinois House passed SB43 on its third reading May 22, 2018. On August 17, 2018, the Governor signed into law SB43 (Public Act 100-0919), amending the Illinois Finance Authority Act as advocated for by the Authority.

In addition to various amendments related to the Authority's rejuvenated Participation Loan Program, SB43 clarifies that a financeable "project" under the Illinois Finance Authority Act is a "PACE Project," which is an "energy project" as provided for under the Property Assessed Clean Energy Act. Within this statutory framework, SB43 further provides that the Authority may utilize its available assets to make loans for Energy Projects, including but not limited to assets in the Industrial Project Insurance Fund, and similarly apply its experience as a conduit bond issuer for long-term bond financing of Energy Projects. Local units of government are not mandated by SB43 to utilize the Authority. Finally, SB43 makes clear that the Authority's previous authorization to issue bonds in an amount not to exceed \$2 billion for Clean Coal, Coal, Energy Efficiency and Renewable Energy Projects also includes Energy Projects.

III. SB2773 – PACE Act Amendment

On April 17, 2018, an amendment to the Property Assessed Clean Energy Act was filed in the Illinois Senate. After receiving recommendation by the Senate Commerce and Economic Development Committee, the Senate unanimously passed SB2773 on its third reading May 2, 2018. SB2773 arrived in the Illinois House of Representatives on May 3, 2018. After receiving recommendation by House Revenue and Finance Committee, the Illinois House passed SB2773 on its third reading May 30, 2018. On August 19, 2018, the Governor signed into law SB2773 (Public Act 100-0980), amending the

Property Assessed Clean Energy Act as advocated for by the Authority. The effective date of the amendment was January 1, 2019.

SB2773 provides that local units of government may assign assessment contracts to any body politic and corporate (such as the Authority), any bond trustee for purposes of properly structuring required legal documents, or any warehouse lender or warehouse fund for purposes of making interim loans for Energy Projects.

By permitting assignment of assessment contracts to the Authority pursuant to SB2773, the Authority can be provided the necessary collateral required to issue municipal bonds for Energy Projects under its own corporate powers (“PACE Bonds”). Issuance of PACE Bonds by the Authority will drive standardization of bond documents and avail a more efficient PACE Bond issuance process, while also reducing legal and operational costs for borrowers, local units of government, program administrators, and capital providers. Furthermore, this standardization will improve liquidity in the Illinois C-PACE market.

SB2773 also accommodates the complexity of financing small Energy Projects by allowing a warehouse lender (i.e., private financial institution) or a warehouse fund (i.e., established by either a local unit of government or potentially the Authority) to make interim loans as long-term bond financing of small Energy Projects may be considered uneconomical. As a result, small Energy Projects can receive immediate interim funding rather than being delayed until a pooled PACE Bond financing can be completed in an economical manner. The pooling of assessment contracts for small Energy Projects together creates economies of scale when issuing a long-term PACE Bond. Importantly, as a statewide body politic and corporate, the Authority can effectively pool these assessment contracts across multiple jurisdictions in a program administrator’s market area for purposes of PACE Bond financing.

SB2773 also improves the enforcement provisions of assessment contracts, necessary for Energy Projects to be financeable in general. Other legislative improvements include availing property assessed clean energy programs for new construction, clarifying what is required when recording a lien with the county clerk as a result of a voluntary assessment contract, making clear that a local unit of government may procure more than one program administrator to incentivize competition, and mandating that any public hearings that may be required by a local unit of government establishing a PACE area must be held by the local unit of government itself to achieve transparency.

Finally, while existing law provides that municipal bonds secured by assessment contracts are never general obligations of taxpayers, SB2773 further restricts any PACE Bonds issued by the Authority from utilizing the moral obligation of the State of Illinois.

Administrative Law:

Previously, on November 13, 2018, Members of the Authority adopted a Resolution approving the proposed repeal, modification, and amendment of existing rules, including implementation of certain new rules, to the Illinois Administrative Code. Specifically, the Authority determined that an emergency exists necessitating the urgent adoption of an emergency rule regarding “Bond Counsel on Pooled Financings.”

The Illinois Administrative Code previously stated that the Authority shall select bond counsel on all pooled financings. However, the Authority reasonably expects some PACE Bond financings to be pooled financings, and likewise asserts that program administrators and capital providers in a pooled PACE Bond financing should be able to engage their own transaction team, including bond counsel.

As a result, an emergency rule is being submitted to the Secretary of State Index Department exempting pooled PACE Bond financings from the mandate that the Authority shall select bond counsel. The emergency rule will remain in effect for approximately 150 days upon its submission.

During the 150-day period, the Authority will be submitting and publishing in its entirety the proposed repeal, modification, and amendment of existing rules, including implementation of certain new rules, to the Illinois Administrative Code.

C-PACE Bond Financing Services; Parameters:

I. Standardized Documents

The Authority has drafted a standardized ordinance local units of government can download from the Authority's website or request from staff in order to establish a PACE area within their jurisdictional boundaries upon selecting a program administrator. The standardized ordinance the Authority avails to local units of government establishes the PACE area, approves the statutorily required program administrator program report, delegates an Authorized Officer (as defined therein) to both execute assessment contracts and assign assessment contracts to the Authority, and approves the form of assessment contract.

The Authority, therefore, has crafted provisions that must be incorporated into a form assessment contract adopted by a local unit of government in order for the Authority to accept its assignment as security for PACE Bond issuance by the Authority.

Accordingly, approval of the Authority's updated Bond Handbook is requested in connection with the Authority's commencement of offering C-PACE bond financing services. Referenced as Exhibit 1 to the accompanying Resolution, the substantially final updates to the Bond Handbook set forth the Authority's requirements and policies applicable to PACE Bonds issued by the Authority, including but not limited to the requisite assessment contract provisions, the PACE Bond application process, and the form of PACE Bond Resolution.

As the standardized form of PACE Bond Resolution in the Bond Handbook to be utilized by any bond counsel will approve a form Master Indenture and related Issuance Certificate, the Authority has expended time and resources drafting a form Master Indenture and form Issuance Certificate in furtherance of upholding standardization principles and fostering diminished legal costs of property assessed clean energy programs across the state. The form Master Indenture and related Issuance Certificate is available to program administrators upon request.

II. Efficient Bond Issuance

The PACE Bond Resolution will approve the maximum term, interest rate and principal amount of PACE Bonds that may be issued by the Authority for purchase by a capital provider for Energy Projects located throughout the state, provided that an Energy Project is located in a PACE area and a program administrator is administering the property assessed clean energy program on behalf of or at the discretion of the applicable local unit of government. Thereafter, Authorized Officers (as defined in the PACE Bond Resolution) may execute Issuance Certificates under the approved form of Master Indenture for the applicable capital provider to finance Energy Projects. This delegation ensures efficient and timely funding of Energy Projects by capital providers consistent with market expectations.

Accordingly, the Authority will have a separate, distinct Master Indenture and related Issuance Certificates for each capital provider in a program administrator's market area. As a result, a capital

provider can fund multiple Energy Projects through a single Master Indenture, improving liquidity in the Illinois C-PACE market as the PACE Bonds issued by the Authority for a particular capital provider are therefore easier to securitize in the secondary market. Multiple Energy Projects can also be financed in a single Issuance Certificate, if necessary, to achieve economies of scale for bond financing of small Energy Projects located in multiple jurisdictions, if applicable.

Upon approval of a capital provider's PACE Bond Resolution, the respective capital provider will submit an application for each Energy Project it wishes to finance through the issuance of PACE Bonds by the Authority. As outlined in the updates to the Bond Handbook, staff will review each application in order for Authorized Officers to execute and deliver the requisite Issuance Certificate and bond closing documents for each Energy Project. Bond counsel will confirm the assigned assessment contract satisfies the requirements detailed in the Bond Handbook of the Authority.

Finally, no PACE Bonds may be issued pursuant to a PACE Bond Resolution for any capital provider more than three years after the approval date of the PACE Bond Resolution. This sunset provision allows the Authority to properly manage its available bonding capacity pursuant to state statute and has the effect of requiring capital providers to seek additional approval for additional bonding authorization as needed.

Authority staff anticipates providing a synopsis of successful PACE Bond closings to Members of the Authority on a quarterly basis, at a minimum.

III. Affordable Fees

Approval of the Authority's Fee Schedule for issuing PACE Bonds is requested in connection with the Authority's commencement of offering C-PACE bond financing services. Referenced as confidential Exhibit 2 to the accompanying Resolution, the Fee Schedule for issuance of PACE Bonds suggests a flat basis point fee (based on an Issuance Certificate's total par amount) for services rendered, provided that there is both a minimum and maximum fee.

There is no application fee for issuance of PACE bonds upon assignment of an assessment contract from a local unit of government. Typically, borrowers have already paid an application fee to program administrators administering the property assessed clean energy program on behalf of or at the discretion of a local unit of government.

Future C-PACE Opportunity: Interim Funding Product

The Authority may at a later time consider dedicating a portion of its unrestricted balance sheet assets from the defeasance of the former Illinois Local Government Bond Bank for interim funding small Energy Projects that are otherwise uneconomical for purposes of long-term bond financing. The goal of the Authority's warehouse fund would be to offer capital providers a low cost of capital while providing borrowers immediate funding, in addition to generating interest income. The interest rate of the Authority's warehouse fund would be designed to drive C-PACE business to the Authority while also minimizing any opportunity costs associated with otherwise investing the Authority's unrestricted balance sheet assets at maximum yield per the Authority's Investment Policy Statement.

Notably, unrestricted assets from the defeasance of the former Illinois Local Government Bond and otherwise restricted monies held in the Authority's Industrial Revenue Bond Insurance Fund (in addition to otherwise restricted monies held in both the Illinois Agricultural Loan Guarantee Fund and the Illinois Farmer and Agribusiness Loan Guarantee Fund) can be made available for interim funding small Energy Projects if needed, ensuring sufficient available capital as the Authority's C-PACE interim funding product develops and matures. Given that the non-operating (investment) assets of the Authority are held

with one custodian, the Authority reasonably anticipates engaging its custodian to serve as the depository for the Authority warehouse fund, the engagement of which may be accomplished as a small purchase by Authority staff.

Recommendation:

Authority staff recommends approval of the accompanying Resolution, including Exhibit1 and Exhibit 2.

Based on the success of the Authority's C-PACE bond financing services and market reaction, staff may request approval of a subsequent resolution to implement a C-PACE interim funding product.

Respectfully submitted,

/s/ Brad R. Fletcher
Vice President

Enclosures: Resolution
Exhibit 1 Updated Bond Handbook
Exhibit 2 PACE Fee Schedule (Confidential)