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Maryland General Assembly  
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FISCAL AND POLICY NOTE

House Bill 603  
Economic Matters

(Delegate Summers, *et al.*)

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Maryland Energy Administration - Clean Energy Loan Payment Program

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This bill establishes a Clean Energy Loan Payment Program (CELPP) in the Maryland Energy Administration (MEA) to finance residential and commercial energy efficiency and renewable energy projects. Loans under the program are repaid through a clean energy surcharge on a property owner's property tax bill. Loan repayments are paid into a Clean Energy Loan Payment Fund established by the bill to be used to provide loans under the bill and to pay the expenses of the program.

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Fiscal Summary

**State Effect:** General fund/GO bond expenditures may increase significantly in FY 2012 and subsequent years to administer CELPP and provide loans under the program. Under one scenario, general fund expenditures potentially increase by at least \$145,900 in FY 2012 to administer the program and general fund/GO bond expenditures increase by \$2.25 million in FY 2012 to provide the loans. State expenditures should decrease in future years to the extent clean energy surcharge revenues become sufficient to sustain the program.

**Local Effect:** Local government expenditures may increase significantly due to any programming changes or additional staff necessary to administer collection of the clean energy surcharge through county property tax systems. **This bill may impose a mandate on a unit of local government.**

**Small Business Effect:** Potential meaningful.

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## Analysis

### **Bill Summary:**

#### *Purpose and Administration of the Program*

CELPP is established to provide low-interest loans to residential and commercial property owners for the financing of energy efficiency and renewable energy projects. MEA must manage, supervise, and administer the program, adopt specified regulations, and attach to any loans specific terms MEA considers necessary to ensure the purposes of the program are fulfilled.

#### *Repayment of Loans through Clean Energy Surcharge*

Loans must be repaid through a clean energy surcharge on the property owner's property tax bill. The Mayor and City Council of Baltimore City or the governing body of a county is not required to pass any law to incorporate the clean energy surcharge in the property tax bill or to collect the surcharge.

The surcharge must be limited to an amount that allows the State to recover the principal of the loan, any outstanding interest on the loan, and costs associated with administering the program. The amount of a loan provided under the program may not exceed 10% of the assessed value of the property according to current county property tax records.

A person who acquires property subject to a clean energy surcharge, whether by purchase or other means, assumes the obligation to pay the surcharge.

A clean energy surcharge, including any interest and penalty, constitutes a lien against the property subject to the surcharge. Any lien created in favor of MEA under the bill is effective against the person against whose property the lien exists; however, a lien does not have priority over a prior secured interest. A lien is also not effective against any third party unless specified written notice of the lien is recorded and indexed as specified in the bill. The bill also outlines procedures related to the release of a lien.

A secured party under a mortgage or deed of trust on the property may collect and hold in an escrow account payments due on loans made under the program in the same manner as the secured party may collect and hold in an escrow account payments for property taxes or insurance for the property.

The liability for the loan assessment in property foreclosures is limited to any amount in arrears at that time. The outstanding balance of a loan may not be accelerated or made due in full.

### *Loan Eligibility/Requirements*

Regulations adopted by MEA must provide for eligibility requirements for participation in the program, including eligibility requirements for energy efficiency improvements and renewable energy devices and for property and property owners. The regulations must also provide for loan terms and conditions.

MEA must, in a manner substantially similar to that required for a mortgage loan under the Commercial Law Article, give due regard to the property owner's ability to repay loans provided under the program in determining eligibility. If a property is subject to any recorded mortgage or deed of trust when the property owner applies for participation in the program, at the time of the application for a loan under the program, MEA must send notice to each secured party under a recorded mortgage or deed of trust by first-class certified mail.

A loan may not be given under the program unless property taxes are current; no outstanding and unsatisfied tax liens are on the property; there are no notices of default or other evidence of property-based debt delinquency for the lesser of three years immediately preceding the application for the loan or the length of time the property owner has owned the property; and the property is current on all mortgage debt.

### *Clean Energy Loan Payment Fund*

The bill establishes a Clean Energy Loan Payment Fund, administered by MEA, consisting of money appropriated in the State budget; money received from any public or private source; interest and investment earnings on the fund; and repayments and prepayments of principal and interest on loans provided from the fund. The fund may only be used to provide loans to eligible borrowers and projects and to pay the expenses of the program.

**Current Law:** Pursuant to Chapter 743 of 2009, local governments are authorized to enact clean energy loan programs similar in nature to the State-level program established by this bill. Under Chapter 743, a political subdivision may enact an ordinance or resolution establishing a Clean Energy Loan Program to provide loans to residential and commercial property owners for the financing of energy efficiency and renewable energy projects. An ordinance or resolution enacted must provide for eligibility requirements for participation in the program and loan terms and conditions.

A property owner must repay a loan through a surcharge on the owner's property tax bill, and a person who acquires property subject to a surcharge assumes the obligation to pay the surcharge. A political subdivision has specified authority to issue bonds to finance loans made through the program.

Chapter 743 does not explicitly address whether a clean energy surcharge established by a local government constitutes a lien on the property and an Attorney General bill review letter indicated that the surcharge does not constitute a lien against the property under State law. The Attorney General indicated, however, that a local law could establish a lien, but pointed out issues that could arise with respect to the priority of the lien and notice to mortgagees or trustees.

MEA is currently charged under State law with administering a number of programs aimed at encouraging energy efficiency and renewable energy projects in the State.

**Background:** Property assessed clean energy (PACE) programs provide a property owner the benefit of being able to finance costly clean energy improvements over time and have the responsibility for the financing payments be tied to the property rather than the property owner.

Concerns were expressed in 2010 by financial regulators about the impacts of PACE loan programs that provide priority lien status for the loans over existing mortgage liens. (This bill specifies that a clean energy surcharge lien *does not* have priority over a prior secured interest.) In July 2010, the Federal Housing Finance Agency (FHFA) issued a statement directing Fannie Mae, Freddie Mac, and Federal Home Loan Banks (government-sponsored enterprises regulated by FHFA that provide more than \$5.9 trillion in funding for the U.S. mortgage markets and financial institutions) to take certain prudential actions relating to priority lien PACE programs. The statement indicated that first liens for PACE loans “represent a key alteration of traditional mortgage lending practice” and “present significant risk to lenders and secondary market entities, may alter valuations for mortgage-backed securities and are not essential for successful programs to spur energy conservation.”

According to the U.S. Department of Energy, as a result of this regulatory uncertainty, many PACE programs in the country are on hold, but some communities are exploring second-lien structures as an alternative to priority-lien PACE programs.

**State Fiscal Effect:** General fund/GO bond expenditures may increase significantly in fiscal 2012 and subsequent years to administer CELPP and to capitalize the Clean Energy Loan Payment Fund. Administrative costs will be incurred to administer the program and a significant amount of funding for the loans is expected to be needed to operate a meaningful and effective program. State expenditures should decrease in future years to the extent loan repayment revenues and administrative cost reimbursement generated from the clean energy surcharge become sufficient to sustain the program.

The bill specifies the fund sources for the program as (1) money appropriated in the State budget to the program; (2) money received from any public or private source; (3) interest

and investment earnings of the fund; and (4) repayments and prepayments of principal and interest on loans provided from the fund. If private capital can be attracted to invest in the program, MEA indicates that State funds may nonetheless be required to establish a “loan-loss reserve” in the fund (a dedicated portion of the fund set aside to offset risks of investment, such as loan defaults) and more resources likely will be needed to manage private investments.

In the absence of funding from other sources, it is assumed general funds will be needed to support initial costs of administration of the program and general funds and/or GO bond funding will be needed to provide loans under the program. To the extent GO bond funds are used to make loans, the issuance of taxable bonds is likely to be required due to federal private activity restrictions on the issuance of tax-exempt bonds. This would increase the cost of the program to the State since taxable bonds are issued at a higher true interest cost than tax-exempt bonds; approximately 150 basis points higher for taxable bonds in the current bond market.

#### *Administration of CELPP*

Administration of CELPP will affect MEA both operationally and fiscally. Existing program and legal resources will be devoted to the program and at least one additional staff person and contractual underwriting and legal services will be needed. The responsibilities of the additional staff person will include: assisting in the drafting and promulgation of regulations, tracking loan approvals and denials, managing applications electronically or manually, assisting with large or more complicated loans requiring custom documents, and answering inquiries from interested property owners.

The bill allows for costs associated with administering the program to be collected through the clean energy surcharge; however, it is not clear how those costs would be recovered – up front, over the life of the loan, or in another manner. If the costs are not fully recovered up front, it is assumed, for the purpose of this fiscal and policy note, that general funds will be needed initially to cover at least a portion of the administrative costs of the program.

*For illustrative purposes*, if 100 loans are made each year, MEA administrative costs may total at least \$145,900 annually. This assumes that underwriting and legal costs associated with each loan will equal \$950, the approximate cost MEA incurs for loans made under the Jane E. Lawton Conservation Loan Program (which provides low-interest energy-related loans to nonprofit organizations, local jurisdictions, and eligible businesses).

## *CELPP Loan Funding*

The amount of initial funding needed for loans will depend on the scope chosen for the program. MEA indicates that the cost of residential energy efficiency improvements and renewable energy installation may average \$10,000 and \$35,000 respectively. If 50 loans are made in fiscal 2012 for residential energy efficiency improvements and 50 loans are made for renewable energy installations, general fund expenditures increase by \$2.25 million to fund those loans. Based on information provided by MEA, this is roughly the minimum amount of loan activity needed to have a meaningful and effective program. Making loans for commercial projects as well as residential projects will likely require either a greater amount of funding or a reduction in the overall number of loans made, as the cost of commercial projects is greater.

**Local Fiscal Effect:** Local government expenditures may increase significantly due to programming changes necessary to facilitate the collection of the clean energy surcharge on property tax bills and a potential need for additional staff to handle inquiries from property owners, communicate with MEA, and otherwise administer the collection of the surcharge. Any increase in expenditures is expected to vary by county.

Baltimore County, for example, indicates programming changes would include altering the format of the county's tax bill to accommodate an additional field and reprogramming lien certification computer programs to identify and itemize loan payments as liens against properties. To the extent local government costs can be reimbursed with money from the Clean Energy Loan Payment Fund, any increase in local government expenditures may be minimal.

**Small Business Effect:** Small business property owners interested in making energy efficiency improvements or installing renewable energy devices may benefit from the program. In addition, small businesses in the energy efficiency and renewable energy industries may benefit to the extent the program increases demand for their services.

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## **Additional Information**

**Prior Introductions:** HB 1236 of 2009, a similar bill, received a hearing in the House Economic Matters Committee, but no further action was taken.

**Cross File:** None.

**Information Source(s):** Maryland Energy Administration, Judiciary (Administrative Office of the Courts), Property Tax Assessment Appeals Board, Maryland Clean Energy Center, Baltimore City, Baltimore and Carroll counties, Office of the Attorney General,

U.S. Department of Energy, Federal Housing Finance Agency, U.S. Department of the Treasury (Office of the Comptroller of the Currency), Department of Legislative Services

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