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Dramatic increase in asset value seen for commercial buildings

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In an increasingly competitive real estate market, commercial buildings with high energy performance outpace their neighbors on operating expenses, rent premiums, occupancy and asset value. By significantly reducing utility costs, upgrades like high-efficiency lighting, HVAC systems and solar energy systems result in dramatically increased NOI and drive new cash flows that are capitalized into asset value.

In Connecticut, the advent of affordable financing programs for energy upgrades such as C-PACE (Commercial Property Assessed Clean Energy), specialized revenue streams for renewable energy (ZRECs), and high energy costs are driving smart commercial building owners to invest in energy improvements. Still, the commercial and industrial real estate appraisal industry is falling behind on properly capturing the value owners are adding to Connecticut's building stock.

"Appraisers need to understand energy-efficient building features and appropriate methodologies to measure reduction in energy-related operating expenses," said

John Brenan, director of appraisal issues at The Appraisal Foundation. "They should be familiar with the market dynamics shaping the economics of energy upgrades for commercial building owners, including financing tools like C-PACE and renewable energy commodity markets like ZRECS, where building owners can capture additional value for their properties. These factors are critical for appraisers to measure market reaction and, as a result, incremental value."

Depending on the nature of the improvements and the depth of cost savings, energy upgrades can markedly increase value from the baseline "as is" valuation, with some properties even seeing increases as high as \$2.5 million. For example, Columbia Elevator recently expanded its operations with a new facility in Bridgeport, Connecticut. Utilizing C-PACE financing, Columbia retrofitted the building with LED lighting, solar, and a biodiesel generator that uses gasified wood waste product from the site as fuel. The Connecticut Green Bank, which administers the C-PACE program, required an "as complete" appraisal as part of the project's financial underwriting. This appraisal demonstrated a 9% increase in appraised value when considering these energy improvements, compared with the value with an "as is" appraisal.

In the last two years, the Connecticut Green Bank has originated and underwritten \$65 million in C-PACE loans. The C-PACE program allows commercial, industrial and multifamily property owners and nonprofits to access long-term, low-interest financing for energy upgrades to their buildings with no money down, allowing them to realize immediate cash flow from energy savings. Using money saved on energy bills, building owners repay C-PACE financing through a benefit assessment charge on their tax bill. Typically spreading out over 20 years, the assessment model makes it easy to finance multiple improvements and realize deep savings. Energy-efficiency upgrades through C-PACE regularly reduce property owners' utility bills by 20 to 40%, with solar energy projects

generally producing savings of more than 50% (and many achieving savings of more than 90%). Programs like C-PACE rely on the underlying value of the property to secure the benefit assessment. The program sets thresholds for debt-to-equity that are acceptable to other banks with a security interest in the property. Competent appraisals are essential for securing financing, particularly to demonstrate additional asset value against which the cost of "deep" energy upgrades may be leveraged. "There is an increasing need for more expert appraisers in this area," said Michael Duffany, senior business banking officer at Berkshire Bank. "The market is moving in this direction, and commercial appraisers must understand how to appropriately value high-energy-performing buildings."

In an effort to provide continuing education for commercial real estate appraisers and property owners, the Connecticut Green Bank and the Renewable Energy and Efficiency Business Association (REEBA) will offer a workshop on March 25 in Hartford, Conn.

The workshop will focus on the increasing importance of appraising commercial buildings with renewable energy and energy-efficiency upgrades. It will also feature the Valuation of Green Buildings: Background and Core Competency guidelines, issued by the Appraisal Foundation, which establishes the minimum standards appraisers must meet to be considered "competent" to evaluate property value adjustments afforded by improvements.

Savvy appraisers will want to take advantage of these tools to prepare for serving the ever-changing commercial real estate market. The state of New York has launched a commercial PACE program, and Massachusetts is nearing the passage of a similar initiative. In other Northeast markets, such as New York City, Philadelphia and Boston, regulators have mandated measurement and disclosure of energy costs in commercial buildings.

"Relative energy performance in these markets will increasingly become a factor in which properties are priced at point of sale," said Bryan Garcia, president and CEO of Connecticut Green Bank. "High-performance energy buildings are the wave of the future in the commercial market."

To register for the March 25 event, please visit www.cpace.com/register

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