



## ELEMENTS OF A WELL-DESIGNED C-PACE STATUTE AND PROGRAM TO ATTRACT PRIVATE CAPITAL AND FOSTER GREATER TRANSACTION VOLUMES JULY 2, 2018

### OVERVIEW

As more states, counties and municipalities launch Commercial Property Assessed Clean Energy (C-PACE) programs, a Working Group of four of the largest C-PACE capital providers—Petros PACE Finance, CleanFund Commercial PACE Capital, Inc., Greenworks Lending, and Twain Financial Partners—is pleased to share the members' thoughts on the key elements of a C-PACE statute and program that are essential to attract private capital and foster greater transaction volumes. The members of this Working Group frequently receive requests for input on how C-PACE programs and statutes should be designed. By endorsing and publishing these shared ideas, the Working Group seeks to help jurisdictions increase the volume of high-quality C-PACE projects and realize the public benefits in energy savings, job creation, investment in building upgrades and economic competitiveness.

### BENEFITS OF C-PACE FINANCING

Authorized by state legislation, C-PACE programs allow a Property Owner to repay the financing for energy efficiency, renewable generation and other building upgrades via a voluntary property tax assessment. Typically, a state or local jurisdiction selects one or more C-PACE Program Administrators (PA) to operate its C-PACE program. C-PACE enables up to 30-year financing for eligible improvements that can significantly increase the value of property without requiring personal or corporate guaranties—and without requiring the assessment to be paid off prior to or upon a sale of the building. C-PACE programs are structured to offer long-term, lower-cost financing that can eliminate or substantially reduce upfront capital expenditures, and in many cases, allows Property Owners to pass-through payment obligations and energy savings to tenants. Eligible items for C-PACE financing typically include lighting, systems controls, roofing, HVAC systems, boilers and chillers, insulation, glazed windows, renewable energy systems, and much more. Some states permit property upgrades such as seismic retrofits, storm resiliency measures, and water-efficiency projects.

### GOALS & CORE PRINCIPLES

The various C-PACE stakeholders—Property Owners, Government, Program Administrators, and Capital Providers—share common goals for C-PACE programs:

- Improved energy efficiency, renewable energy deployment, reduced energy consumption, and other improvements deemed to be in the public interest, such as seismic retrofits, storm resiliency measures, and water efficiency in commercial buildings.
- Transparency and simplicity of program implementation and administration.

- Delivery of long-term, lower-cost financing to the Property Owner that better matches the financing costs with anticipated benefits of the improvements over their expected life.
- Local economic development and vitality.
- High usage and project volume.

These shared goals lead to the core principles that apply to well-designed C-PACE programs.

1. **Continuous collaboration:** C-PACE stakeholders should collaborate on a continuous basis to achieve common goals.
2. **Input from stakeholders:** Policymakers should engage a broad set of stakeholders and take into account best practices learned from other statutes and programs as they craft and amend C-PACE legislation.
3. **Open-market philosophy / freedom of choice:** C-PACE programs should encourage open and free-market competition among Capital Providers, project developers and contractors rather than bundling of services.
4. **Focus on implementation:** Once a well-designed statute is enacted, policymakers should provide support and guidance to the local governments that implement a C-PACE program: Municipal ordinances must be adopted and the program supervision must be put in place, which requires considering the role and financial sustainability of a Program Administrator.
5. **Converge on standards:** The C-PACE capital providers should help the industry move toward voluntary standards to ensure the most efficient, flexible and low-cost access to capital – especially as it relates to matters that can expedite the creation of a liquid secondary market for C-PACE assets.

#### ELEMENTS IN THE C-PACE AUTHORIZING STATUTE AND PROGRAM PROVISIONS

1.	<b>Open Market:</b> Encourages an open market for qualified Capital Providers, project developers and contractors to compete for C-PACE projects. The statute should not favor or disadvantage a party in a C-PACE project, although programs may wish to set reasonable minimum qualifications for Capital Providers. If Property Owners are required to obtain an analysis of estimated energy savings, the program should establish qualifications for service providers and foster open-market competition to control costs.
2.	<b>Strong Credit Security:</b> Establishes that C-PACE financing entails a special tax assessment on the property with certain attributes to create a strong form of credit security: <ol style="list-style-type: none"> <li>a. Provides that the assessment has a first and prior lien against the real property on which the assessment is imposed should the taxes be unpaid.</li> <li>b. Possesses the same priority status as a lien for any other <i>ad valorem</i> tax. If this is not possible due to political realities, the C-PACE benefit assessment should be subordinate to property taxes but senior to all other government assessments.</li> <li>c. Becomes effective <i>as of the funding of a project</i>, including lien placement prior to any construction period.</li> </ol>

	<ul style="list-style-type: none"> <li>d. Once approved by the PA and recorded, may not be contested on the basis that the improvement is not a qualified improvement or the project is not a qualified project.</li> <li>e. Non-extinguishable, non-rescindable and non-accelerating.</li> <li>f. May be enforced by the local government in the same manner that a property tax lien against real property is enforced.</li> <li>g. Does not allow for partial payment of property taxes or C-PACE repayments unless such partial payment represents a voluntary prepayment.</li> </ul>
3.	<p><b>Mandatory Approval by Senior Mortgage Holder:</b> Requires approval from all mortgage holders to a C-PACE assessment via written consent or written acknowledgement prior to closing. The senior mortgage holder’s written approval should include a detailed description of the C-PACE financing and a written certification that the financing does not create an event of default under the terms of the mortgage. Simply providing notice of the financing to senior mortgage holders is not sufficient.</p>
4.	<p><b>No Savings-to-Investment (SIR) Threshold:</b> The Working Group recommends that a statute <u>not</u> require a minimum SIR threshold. This recommendation is based on several considerations:</p> <ul style="list-style-type: none"> <li>a. If the price of energy is low and fluctuating, complying with an SIR test is more difficult;</li> <li>b. an SIR test overlooks the other public benefits in a project such as resiliency, increased building code compliance, healthier work environments, and increased tenant retention;</li> <li>c. an SIR test may not account for the full benefit of a lower cost of capital; and</li> <li>d. in states where gut rehabilitation or new construction is eligible for C-PACE, the marginal energy savings over a hypothetical baseline may be wholly inadequate to cover the cost of those improvements, thus undercutting a valuable policy tool that could motivate owners to build higher efficiency buildings.</li> </ul> <p>Finally, landlords may be able charge higher rents for highly energy-efficient space, offsetting a the SIR. For these reasons, the PA should be empowered to approve projects regardless of its SIR.</p> <p>Some programs have used SIR as a rough proxy for determining the property owner’s ability to pay. Standard financial underwriting metrics that capital providers typically employ on a consistent basis (such as a debt service coverage test) are more appropriate to assess creditworthiness, and are often what the mortgage lender will utilize in evaluating the project to provide consent or acknowledgement. Simply put, if an owner and the property itself have the financial wherewithal to cover the cost of the improvements, C-PACE Programs should encourage this behavior and look to other financial underwriting checks and mortgage lender consent to guide project financing amounts.</p> <p>If state or local government applies an SIR test, or requires an SIR calculation, the following should be taken into account:</p> <ul style="list-style-type: none"> <li>a. The estimated savings over the life of the project should include: <ul style="list-style-type: none"> <li>i. Utility savings</li> <li>ii. Operations &amp; maintenance savings (net avoided spending attributable to the new equipment)</li> <li>iii. Avoided capital costs (if the replaced equipment is nearing the end of its useful life)</li> <li>iv. Avoided fees or penalties</li> <li>v. New revenues from renewable energy sources</li> <li>vi. Project financial savings where the C-PACE funds displace higher cost capital</li> <li>vii. Other monetized benefits such as tax credits, utility incentives and rebates</li> </ul> </li> </ul>

	<p>b. The Capital Provider should be tasked to make the SIR calculation based upon program requirements and a consistent approach in determining the SIR value. The PA should review such calculation, but not be required to duplicate the efforts of the Capital Provider in determining the SIR.</p>
5.	<p><b>Flexibility in Financing Terms:</b></p> <ul style="list-style-type: none"> <li>a. Allows for the term of the financing to match the useful life of the equipment, up to 30 years as allowable by law. This flexibility reduces the repayment burden for long-lived property upgrades.</li> <li>b. Allows for renewable energy power purchase agreements or leases to be eligible for C-PACE financing or collection via the benefit assessment mechanism, which promotes greater adoption of renewable energy technology.</li> <li>c. Refrains from setting specific financial underwriting parameters, thus allowing capital providers to use their own standards to confirm ability to repay.</li> <li>d. Allows C-PACE financing to include the cost of materials and labor necessary for equipment installation, permit fees, inspection fees, application and administrative fees, bank fees, maintenance fees, interest reserves, origination fees, and all other fees and costs incurred by the property owner pursuant to the financing and the project.</li> </ul>
6.	<p><b>Billing and Collection Process:</b> Identifies the representative of the local government and the tax assessor empowered to collect the C-PACE assessments without personal liability, or alternatively, allows the Capital Provider to bill and collect from the Property Owner directly. The timeframe between collection of C-PACE payments and remittance to Capital Providers should be minimized, and in any event, no longer than 30 days. Long remittance periods increase costs to the Property Owner.</p>
7.	<p><b>Program Administrator Permitted:</b> Allows a local government to hire (or contract for) and set a reasonable compensation for professional services necessary to administer a program.</p>
8.	<p><b>Statewide Consistency:</b> Ideally, encourages program uniformity by creating a statewide program or “district” that local governments can opt into. This multi-jurisdiction structure facilitates valuable consistency if the PA adopts best practices.</p>
9.	<p><b>Foreclosure Process:</b> Provides clarity and visibility into the foreclosure process for the assessment and a reliable mechanism to ensure timely commencement of foreclosure.</p>

**BEST PRACTICES IN PROGRAM ADMINISTRATION**

1.	<p><b>Clarity of Roles:</b> The PA and the Capital Provider should have clarity about their roles and responsibilities, which some programs memorialize in a signed contract. The PA’s scope of work should focus on three essential functions to minimize cost and encourage open-market competition:</p> <ul style="list-style-type: none"> <li>a. Design the local program rules</li> <li>b. Certify projects that are eligible and compliant</li> <li>c. Promote the program to stakeholders</li> </ul>
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	<p>Capital Providers should perform four key functions:</p> <ul style="list-style-type: none"> <li>a. Cultivate (or Develop) projects / financing opportunities</li> <li>b. Apply project underwriting standards consistently and efficiently</li> <li>c. Coordinate with PAs in the approval, closing, and collection process</li> <li>d. Provide capital to fund projects at competitive rates</li> </ul>
2.	<p><b>Program Administrators’ services should be priced <i>a la carte</i>.</b> A PA that offers services the Property Owner can buy on the private market—such as estimating energy savings, overseeing project development, or evaluating alternative equipment installations—should be priced individually. Separate pricing encourages competition and choice. PAs should disclose to the public if they have a financial interest in these service providers, and Property Owners should have the option of purchasing these services from any qualified provider.</p>
3.	<p><b>Program Administrator Fees and Local Government Fees:</b> PA fees should be reasonable and appropriate in light of various factors such as the size and maturity of the C-PACE market in the subject state. PA fees structures sold as “no cost to the taxing district, paid for by the borrower” can unintentionally thwart C-PACE transactions if these fees are too high. Many successful programs operate with relatively low administration fees, capped per-transaction. For instance, some programs have fees set at 1 percent or less, with per-transaction caps of \$75,000 or less. PAs need financial support to cover staff costs until the transaction volume is sufficient to offset these expenses. Some PAs obtained start-up grants from philanthropies, utility companies or the state; other PAs benefited from loaned executives, donated offices, or consulting revenue. Low fees can help new C-PACE markets grow faster, enabling the PA to reach financial sustainability more quickly. Interest rate “add-ons” during the life of the C-PACE financing are another fee that should be discouraged or be absolutely minimal; generally, a PA’s fees should decline over time as project volume increases. In order to keep fees reasonable, the PA should perform only the functions necessary for project approval and administration.</p>
4.	<p><b>Creating Program Documents:</b> The PA should collaborate with Capital Providers in creating the program documents and the application process, and before changing any of the documentation requirements. The Working Group recommends that the PA convene stakeholder advisory groups to solicit input.</p>
5.	<p><b>Certification of Project Compliance:</b> The PA or the local unit of government should provide a written statement on request that the C-PACE financing for a particular property meets the program requirements.</p>
6.	<p><b>Fair Access by Capital Providers:</b> The PA should do business on the same impartial terms with any party that submits an application. A Capital Provider should be able to submit applications to any PA on the same terms and conditions, including situations where the PA is itself affiliated with a Capital Provider.</p>
7.	<p><b>No Preference among Capital Providers:</b> PAs should not guide a Property Owner to a specific Capital Provider. PAs should refer Property Owners to a list of qualified Capital Providers using a standard template. If a C-PACE program is administered exclusively by one PA, it is desirable that the PA not be affiliated with a Capital Provider. If the PA is affiliated, the Capital Provider/PA</p>

	should deal with all other Capital Providers on an impartial, equal basis, taking special care to avoid appearance of conflicts of interest by documenting the intake and handling of inquiries.
8.	<b>Obtaining Energy Savings Estimates:</b> The PA should encourage Property Owners to obtain an estimate of the potential energy savings from a qualified third-party firm. (As noted above, the Working Group believes an energy analysis should be for the Property Owner’s information rather than an SIR test to determine eligibility for C-PACE financing.) The PA should set the qualifications for the third parties approved to perform this work. If the analysis is required by statute, the PA should review the quality of the energy engineer’s technical work. Some PAs have staff expertise to perform energy savings analysis. However, the PA should price this service <i>a la carte</i> and should not favor its services over other qualified external firms.
9.	<b>Underwriting by Capital Providers:</b> Allows Capital Providers to perform the financial underwriting to confirm the Property Owner’s ability to repay the assessments. PAs should not do any financial underwriting, because it duplicates the Capital Providers’ work with no marginal benefit.
10.	<b>Financing Agreement from Capital Provider:</b> A program should permit a Capital Provider to tailor its financing agreement to meet the needs of the Property Owner and institutional investors, as long as the agreement complies with statutory and program rules. PAs should provide a checklist of statutory and local requirements that must be incorporated.
11.	<b>Efficient Closing Process:</b> Creates a closing process that is predictable, transparent and efficient. Most Capital Providers transfer the C-PACE financing to a secondary institutional investor after closing, so a smooth transfer process is also important. When the PA and Capital Providers can set reliable closing dates, planning and efficiency improves significantly. Predictability is crucial for Capital Providers and investors. The closing process must also be in a proper order for Capital Providers, for example, the tax assessment must be in place before (or contemporaneously with) the project’s funding.
12.	<b>Property Owner’s Satisfaction with the Work of Third Parties:</b> A program should acknowledge that Property Owners are solely responsible for the selection of contractors and any other third parties involved in completing their projects.
13.	<b>Billing Timeframe and Fees:</b> If C-PACE repayments are billed with the regular property tax bill, tax collectors should establish timeframes and reasonable fees for receipt of C-PACE repayments and for remittance to the Capital Provider. The procedure and timeline for the remittance of funds collected by tax assessors to Capital Providers should be included in either the enabling PACE law, the tax assessment document recorded on the property records to evident the PACE assessment, or both.
14.	<b>Continuous Improvement:</b> The PA should lead the design and periodic review of the process to submit applications, determine program eligibility, and obtain approvals. PAs should avoid creating rules that are impractical or high-cost. Contracts between the municipality and PAs should specify minimum acceptable levels of service performance, with the ability for PAs to be replaced for repeated failure to deliver services in a timely manner or adhere to the program guidelines, roles and responsibilities (preferably as outlined in this document).

15.	<b>Standard Form Assessment Contract:</b> If applicable, the PA should help create and maintain a standard form of tax assessment contract (or similar) between the local unit of government and the Property Owner that clearly defines the method of collection of assessments.
16.	<b>Procedures for Delinquencies and Foreclosures:</b> The PA should provide clear guidance on (a) the process for curing delinquencies and (b) the foreclosure process to enforce the C-PACE assessment and rights. Ideally, this process involves a contractual obligation to file a foreclosure action or sell a tax certificate with minimal delay, and allows the right to pursue remedies to be assigned to the Capital Provider. The PA should publish a program handbook setting forth the collection and foreclosure processes and timelines.
17.	<b>Payments Process:</b> For those transactions and related payments that are not received by the Capital Provider through direct billing, collection of C-PACE payments should be into a controlled lockbox, with a third-party remittance firm ensuring proper flow-through of payments to the Capital Provider. The design of a remittance framework should ensure that funds will not be lost, stolen or displaced.
18.	<b>Replicability:</b> The PA should develop a turn-key program (with documents available on its website) that other counties and municipalities within the state can adopt.

**ELEMENTS IN MARKETING, EDUCATION & TRAINING**

1.	<b>Message:</b> The marketing message should emphasize that C-PACE is an alternative financing tool, as well as a means to promote the adoption of renewable energy and efficiency projects.
2.	<b>Marketing (General Awareness of C-PACE):</b> If resources and time permit, the PA should raise local community awareness of the C-PACE program through websites, flyers and local media. The private stakeholders should help market C-PACE as well.
3.	<b>Education (Explanation of C-PACE Financing and Approval Process):</b> The PA should offer seminars and speak at public events to explain the program to Property Owners, contractors, and economic development organizations. Stakeholders should assist with education.
4.	<b>Training (For Qualified Energy Savings Analysts or Project Developers):</b> If the PA keeps a list of qualified third-parties to conduct energy savings analysts or project development, then the PA must take responsibility for organizing technical training for contractors and engineers. These services can be paid for with a separate fee to contractors and engineers to cover the PA costs.

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