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KEEPINGPACE

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Property Assessed Clean Energy (PACE) is an innovative financing mechanism in the U.S. that allows property owners to fund energy-efficiency upgrades with no up-front capital investment on their part. In brief, the investment is funded by a PACE lender with re-payment structured as an assessment to the property's annual tax bill. PACE is adopted through legislation at the state level, and then depending on the state regulations, cities and/or counties opt in to the program.

PACENATION SUMMIT

The second annual PACENation Summit[1] was held in Denver, Colorado, USA, Feb. 13-15, 2017. PACENation[2] is a non-profit organization whose mission is to promote the PACE funding mechanism across the United States. There were more than 450 attendees at this year's conference from across the U.S., Canada and even Spain. The conference agenda predominantly emphasized the funding aspects of commercial and residential PACE while advancing a clean energy agenda and environmental stewardship.

Currently, 33 states, plus Washington, D.C., have adopted PACE for commercial and/or residential programs. For example, Colorado adopted commercial PACE in 2016, with residential PACE still under evaluation. The state is now going through the process of local jurisdictions opting in. Boulder, Colorado, USA, was one of the first jurisdictions to opt in, and the City and County of Denver opted in to the program in September 2016.[3]

Since its inception in 2009, PACE has witnessed a steady rise, reaching 1,020 projects and US$340 million in funding through 2016. While many states are still in the adoption phase of the program, California leads the pack with nearly 500 projects topping US$130 million in funding. Most projects funded to date are for office buildings, however, projects do span the full range of property categories.

How do I get started?

While PACE funding is limited to energy-efficiency upgrades, it is very flexible with eligibility for incorporating related project components. For example, if you want to install a solar array on a rooftop, but the roof would need be replaced first due to its age, then PACE would generally approve incorporation of the roof replacement as part of the funding package.

The best way to explore eligibility for PACE funding is to engage an energy-efficiency contractor. Using the PACENation webpage and PACE Programs Near You[4] as a reference, you'll find that each state generally has a web presence to explain its program and provide references to local resources. For example, the Colorado C-PACE website maintains a directory of C-PACE registered contractors.[5]

While there are no special licensing requirements, these contractors are familiar with the PACE program guidelines and will be able to determine eligibility for project components. The energy-efficiency contractor will typically evaluate (audit) a range of efficiency upgrade options, and model projected energy savings to compare against the capital funding requirements. The goal is for PACE-funded projects to return annual energy cost savings greater than the annual assessment placed on the property tax bill.

Energy-efficiency contractors may also have relationships with one or more PACE lenders who would not only provide the funding, but work with the various stakeholders to explain the program and its financial benefits. Lastly, the energy-efficiency contractor may have one or more trade contractors who will implement the upgrades after funding has been secured. Measurement and verification following project implementation is generally a requirement to ensure the designed efficiency upgrades have been achieved.

Do I need lender consent?

Most commercial properties have at least one mortgage, and therefore a mortgage lender. The mortgage lender will be concerned with any new financial liabilities placed on the property and how it affects their position should something go wrong (e.g., foreclosures, bankruptcy, etc.).

Consequently, most mortgage contracts have language requiring lender consent to any new financial liabilities against the property. The mortgage lender typically holds the senior position (first in line) to get paid in cases of financial default. However, the tax authority will come in ahead of the lender to collect any delinquent taxes.

With respect to any PACE tax assessments on the property, there is no requirement to accelerate payoff of the PACE-funded assessment. This is a noteworthy advantage, as the property can be sold without a need to retire the PACE debt as a part of the sale — as would be the case with typical power purchase agreements or on-bill utility financing programs.

In most cases, the mortgage lender may only be at risk for a one-year assessment amount. Since the energy-efficiency upgrades often increase the value of the property, mortgage lenders are more inclined to consent to PACE funding requests once they understand the benefits and administration of the program.

What about new construction?

While PACE was originally envisioned to fund energy-efficiency upgrades to existing buildings, some recent new construction projects have been able to incorporate PACE funding for energy-efficient building systems into the overall project "capital stack."

Many new construction projects require more than one source of funding in order to complete the project, otherwise known as the capital stack. Developers have found innovative ways to take advantage of the PACE funding mechanism to reduce mortgage debt and construction loan funding, also known as mezzanine debt. This lowers the individual risk to mortgage lenders and contractors.

What if I'm leasing a property?

PACE does incur an assessment against the property taxes, so the building owner must always be party to a PACE funding initiative. However, a property tenant may find value in partnering with the building owner to seek out energy-efficiency upgrades. Under a full-service lease, the building owner would likely accrue most of the energy-efficiency upgrade cost reductions. But if the tenant is paying a pro rata share of the building utility expenses, those cost savings might be passed on.

For triple-net leases, the tenant may be more motivated to seek out energy-efficiency upgrades as the building maintenance and utility costs are likely their responsibility. In this case, most of the energy-efficiency benefits would accrue to the tenant. If the upgrades increase the value of the property, that benefit accrues to the owner. While leasing scenarios are more complex due to the number of stakeholders that must be involved, it can still result in a win-win situation for the tenant and the owner.

Why isn't everyone using PACE funding?

While PACE funding awareness is growing, it is still fairly unknown. In U.S. states like Colorado, where the legislation is relatively new, the PACE contractor and lender market is just getting started.

For facility managers, PACE may present an innovative mechanism to get funding for long-delayed building upgrades with no out-of-pocket capital requirements. Every facility manager should learn more about PACE legislation in progress or programs already available in his or her state.

If programs are available, determine if they may be a good fit for your organization. Not only will you knock off some of that maintenance backlog, but it may also make you a hero for delivering a significant annual expense reduction to your company. FMJ

REFERENCES

1. pacenation.us/summit-2017
2. pacenation.us
3. You can learn more about Colorado's C-PACE program at copace.com.
4. Visit the PACENation website to view PACE Programs Near You (pacenation.us/pace-programs) and learn more about programs in other states.
5. copace.com/contractors/directory-of-contractors

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