CREFC
C-PACE PRIMER

CREFC 30 YEARS
CRE FINANCE COUNCIL

WHAT IS COMMERCIAL - PROPERTY-ASSESSED CLEAN ENERGY (C-PACE) OR C-PACE(R) (RESILIENCY)?

C-PACE is a municipal program that enables private capital to fund CRE sustainability or resiliency improvements on new and existing buildings. Improvements include but are not limited to:

- Equipment and installation costs for energy efficiency projects like HVAC, efficient windows and doors, control systems, roofing, elevators.[1]
- On-site renewable energy systems, such as solar panels or geothermal systems.[2]
- Water conservation and efficiency improvements, such as low-flow fixtures, landscaping, or irrigation systems, eligible in some states.
- Enhanced protection of buildings from climate-related weather risks in selected states and/or greater resiliency such as seismic strengthening improvements in California, Oregon, Washington, and Utah, wind resiliency in Florida, and stormwater/flood management in much of the mid-Atlantic.

Covers up to 100% of the cost of a retrofit-related project, including all related work and soft costs, typically limited to 25%-35% of the property's valuation, in some cases by state law. Most C-PACE programs require third-party audits to substantiate the amount of C-PACE financing being provided by verifying the eligibility of financed measures.

Can also be used to fund components of new ground-up construction or major "gut rehab" projects:

- Typically represents 25%-40% of total project vertical construction[3] costs.

Financing of projects post-completion, up to three years in most states, is also permitted.

Generally, secured by a non-ad valorem special assessment and imposed on the property by the taxing authority. The capital provider or program administrator is responsible for collecting the payments. Alternatively, the local taxing authority may collect repayments along with other property taxes and forward to the C-PACE investor or the designated trustee or agent.

[1] Eligible in all states.
[2] Ibid.
[3] Includes soft costs like engineering and permitting.

WHO HAS JURISDICTION OVER C-PACE?

C-PACE is a public-private partnership, enabled by state law and customized through adoption of local ordinance.

State-level legislation establishes the broad categories of sustainability and resilience improvements that constitute public benefits and authorizes municipalities and/or counties to levy assessments.

- State law usually prescribes a state-wide administrative framework to which all local governments 'opt-in.'
- In some instances, state law prescribes that local governments that establish a program can do so locally or via participation in a regional governing body.

40

STATES AND D.C. HAVE ENABLED C-PACE THROUGH LEGISLATION

75

ACTIVE C-PACE PROGRAMS THROUGHOUT THE COUNTRY

Currently, more than 40 states and D.C. have enabled C-PACE through legislation.[4] There are over 75 active C-PACE programs. In some cases, there are multiple local programs in the same state. Programs can vary significantly across and within states, which can be challenging for both property owners and C-PACE capital providers.

- Most C-PACE programs require capital providers to be registered with certain qualifications, including experience and operation across multiple C-PACE programs.

Certain Federal agency lenders have also approved the program and issued specific guidance for underwriting alongside C-PACE: USDA, HUD (multifamily), SBA 7a, and Freddie Mac.

- Although Freddie Mac's C-PACE guidance was published many years ago, the Enterprise has not yet approved a transaction.
- Fannie Mae, SBA 504, HUD Healthcare and Multifamily (new construction only) have not yet consented to C-PACE. Concerns about residential (single family) C-PACE (largely consumer protection and transparency-related issues) complicate FHFA consideration.

Note that in many states and by most C-PACE capital provider underwriting policies, if a first-mortgage lender is in place prior to the addition of the C-PACE financing, the first-mortgage lender must be notified in advance and must execute a "lender consent" document.

- Only the portion of the C-PACE assessment that is currently due or delinquent is senior to the first-lien position, and the unpaid (not currently due) amount of the C-PACE assessment will not be extinguished by the foreclosure of any existing or future first mortgage.

[4] https://www.energy.gov/scep/slsc/property-assessed-clean-energy-programs#:~:text=Commercial%20PACE,-C%2DPACE%20programs&text=local%20programs)%2C%20financing%20structures%2C,in%20projects%20have%20been%20financed

TYPICAL TERMS FOR A C-PACE FINANCING?

Terms are negotiated with C-PACE Capital Provider

- **Financing provides up to 100% of hard and soft eligible costs**
- **Long-term financing is typically 25-30 years; fixed interest rates**
  - C-PACE is always self-amortizing. Final principal balance must be $0 at term.
  - Generally, have option for capitalized interest provisions (up to two years) and interest-only periods (up to five years)[5]
- **Repayments made at same time as property taxes (unless assessment is off tax bill)**
  - Prepayment allowed (with call protection in early years)
- **Secured by a property lien (not a personal guarantee)**
- **Lien enforcement and foreclosure remedies occur solely in events of non-payment of the C-PACE assessment and typically follow same process as other property taxes.**
  - Non-accelerable in the event of default, but any amounts unpaid/delinquent at a particular moment prime the senior mortgage.
- **In the event of a tax sale or other ownership change, the C-PACE assessment becomes an obligation of the new property owner.**
  - The new owner is required to bring any unpaid C-PACE assessments current, but is not obligated to repay the outstanding principal balance of a C-PACE loan. May prepay, typically with penalty, the C-PACE assessment voluntarily.

[5] Often dictated by capital provider's underwriting policy.

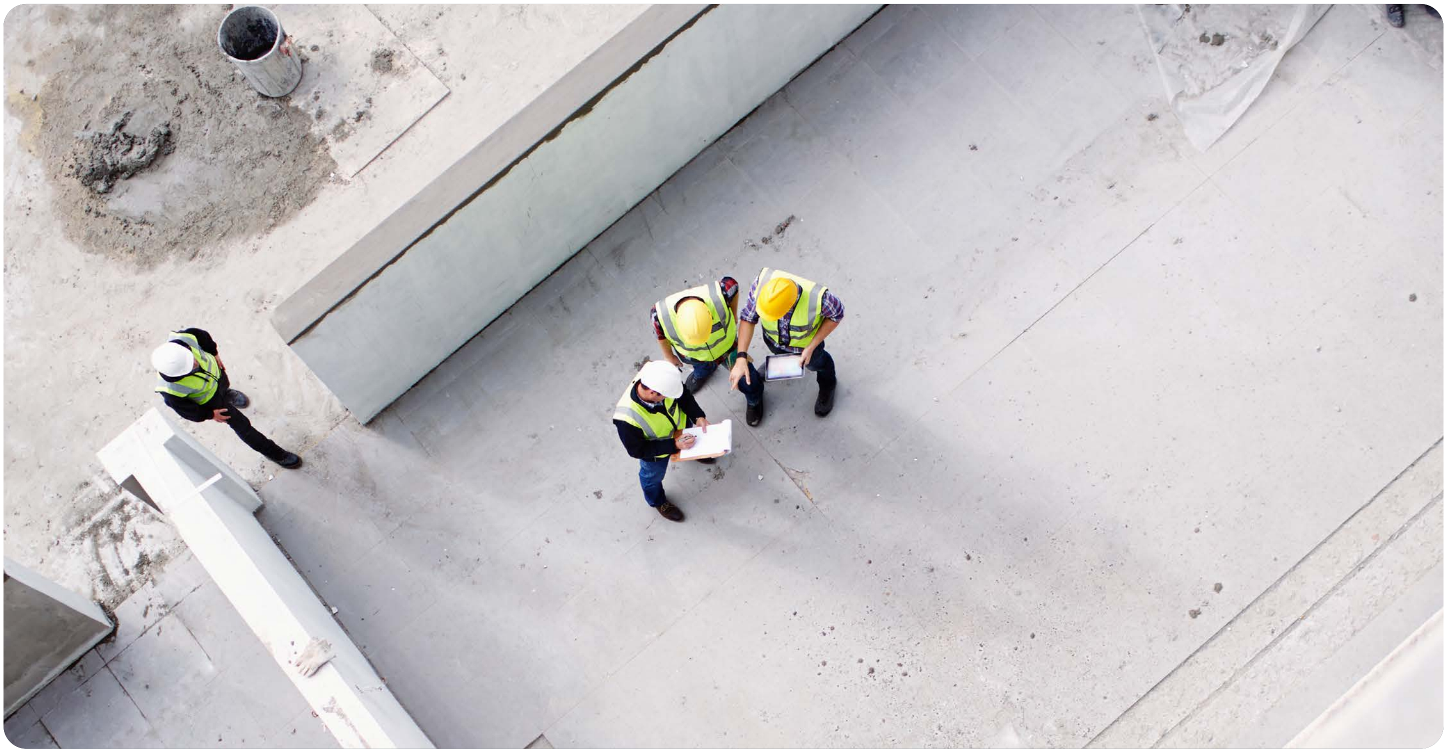
INVESTOR CONSIDERATIONS

Percentage of C-PACE in the capital stack

- Typically, 5%–25% of the property's value, together with the first mortgage not exceeding an all-in 75%–90% LTV. Note that some C-PACE capital providers and C-PACE programs allow higher C-PACE LTVs, possibly up to 35%, subject to senior lender consent.

Cash management

- For construction financing, C-PACE capital provider controls fund disbursement as eligible costs occur; in some instances, the program authority must approve the final disbursement.
- Up-front and ongoing reserves to cover C-PACE payments.
- Capitalization of I/O payments due to the C-PACE capital provider allowed until the tax assessment can be placed on the tax rolls and/or until a project is completed and/or stabilized. Interest accrual between closing and first repayment date is determined for each project individually (amount of capitalized interest can be large).
- Same notice and cure rights as other property taxes in the event of non-payment. Strict notice and cure rights with respect to a property-owner default.
- C-PACE default as a carveout guarantee from the borrower's non-recourse provisions with other lenders.



INVESTOR CONSIDERATIONS (CONTINUED)

Underwriting considerations

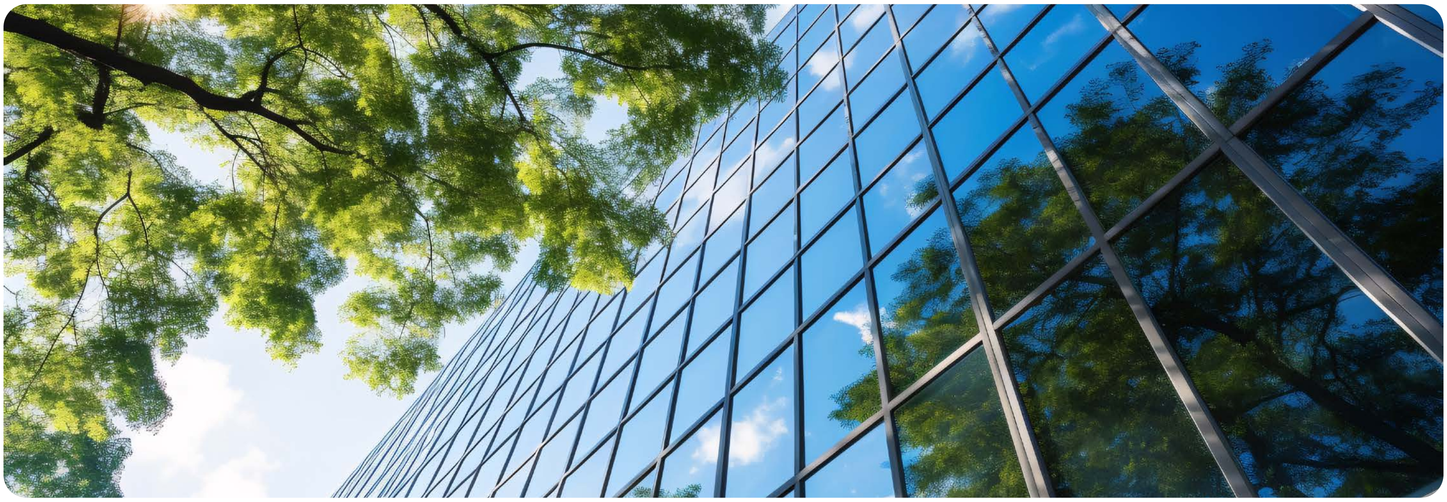
- Most market participants consider C-PACE to be debt. It is voluntary, can be paid off in a lump sum, and cannot be accelerated in a bankruptcy of the property owner.
- All lenders incorporate C-PACE into their DSCR calculation.
- Underwriting is akin to a ground lease, with the benefit that C-PACE is prepayable at par (with call protection in early years) and otherwise fully amortizes. However, unlike ground leases, C-PACE financing is term limited.
  - Treat the assessment as an expense like property taxes, particularly if the C-PACE assessment is small.

Lease considerations

- Depending on lease drafting, C-PACE payments may be a pass through or capable of recapture as a tax escalation.

CMBS loan documents

- In general, C-PACE is not permitted in CMBS. Standard-form CMBS loan documents historically have prohibited C-PACE.
- Recently, however, a few CMBS transactions allow for property owners to enter into C-PACE financing in the future.
  - These documents typically limit C-PACE to a small dollar amount, and require lender's approval and rating agency confirmation.
  - Rating agencies have indicated that the incorporation of C-PACE can be considered if approved by existing mortgage lender.



OTHER STAKEHOLDERS

Counsel

Counsel typically assists the C-PACE capital provider in ensuring its template documents and closing processes and procedures comply with the C-PACE program's rules and regulations, as well as any C-PACE legislation. Some C-PACE capital providers also will obtain legal opinions from local counsel on the viability of a C-PACE program before providing financing through it.

Property Owners

Typically, only the owner of record on private property may enter into an agreement with the taxing authority. This property may be non-profit ownership or could be subject to a ground lease. Some locations also allow public property and leasehold interests to enter into an agreement with the taxing authority.

Certain buyers are not willing to assume a C-PACE assessment upon purchase of a property; they would therefore consider the purchase as requiring a prepayment (sometimes with penalty) of the C-PACE assessment.

Tenants

Tenants request landlords to finance energy-generation projects and generators through C-PACE with financing term tied to the remaining term of the lease. Off-grid power sources prevent business interruption during power outages.

Construction Industry

Increases job creation for energy projects.

Administrators (Representing Public Interest)

Administrator may be a local government official, an authorized representative, a green bank that also functions as a C-PACE capital provider, or a capital provider who enters into a bond indenture with a bonding and taxing authority.

Master Servicers (or Trustees / Title Companies)

Monitor C-PACE assessments, collections, and disbursements.

Mortgage Lenders

Mortgage lenders secured by a property must provide consent to C-PACE before it can be levied against such property.

Third-Party Cost Reviewers (Construction and Gut Rehab Projects)

Most C-PACE capital providers rely upon the third-party cost review obtained by the mortgage lender. However, if the mortgage lender does not obtain one, many C-PACE capital providers will obtain their own third-party cost review.

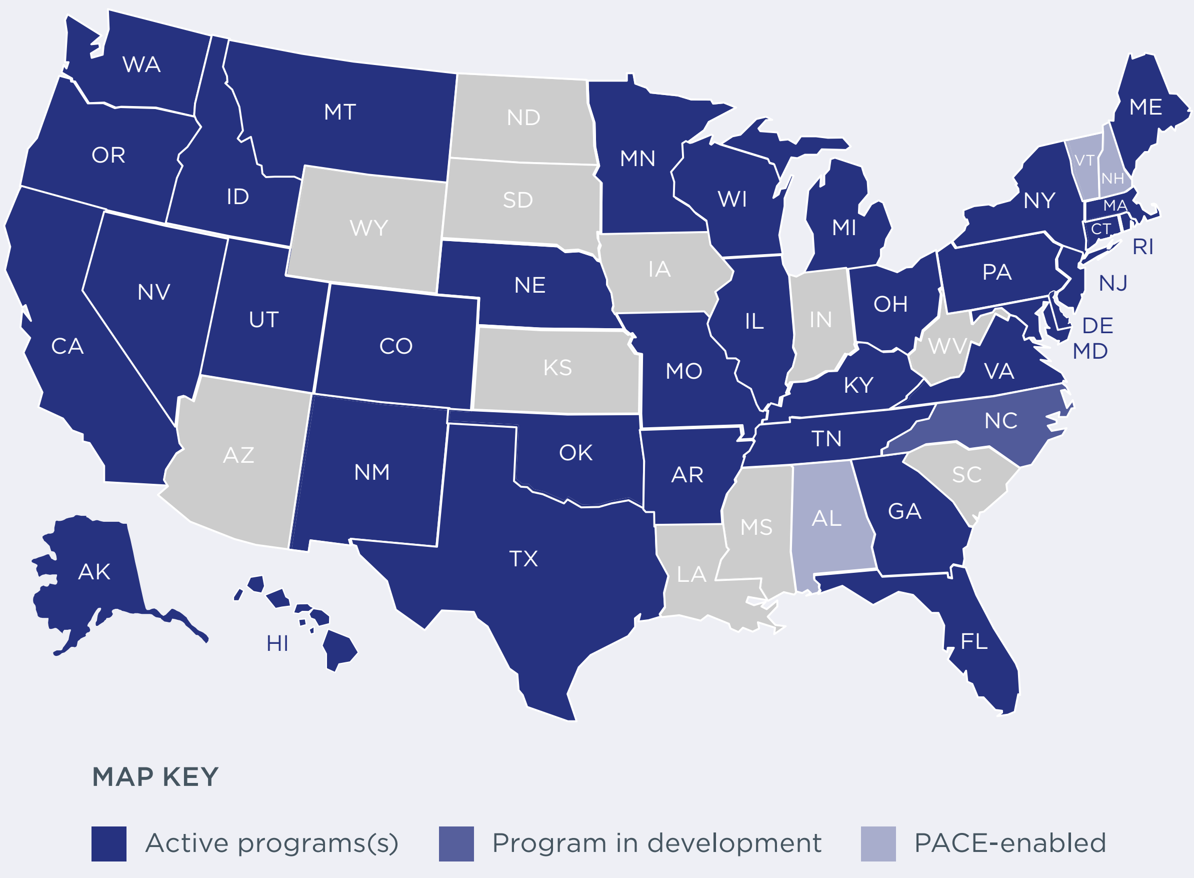
CURRENT MARKET TRENDS

According to a 2023 C-PACE Alliance (a "nonprofit network committed to increasing the volume of quality C-PACE projects") survey[6]:

TOTAL NUMBER OF C-PACE PROJECTS:
OVER **2,300**
AND
$7 BILLION
IN FINANCING ACTIVITY

TOTAL NUMBER OF C-PACE PROJECTS IN 2023
NEARLY **250**
AND
OVER **$2 BILLION**
IN FINANCING ACTIVITY

The below map from Pace Nation shows C-PACE status across the U.S.[7]



[6] https://c-pacealliance.org/c-pace-program-volume/
[7] https://www.pacenation.org/pace-programs/