



## Benefits of Providing Mortgage Lender Consent for a C-PACE Project

The Efficiency Maine C-PACE Program, a finance initiative of the Efficiency Maine Green Bank, is available for qualifying projects located within participating municipalities. C-PACE, which stands for Commercial Property Assessed Clean Energy, provides access to loans for commercial property owners interested in undertaking energy efficiency and clean energy improvements on their buildings. This resource is available to help the local lending community better understand what it would mean to participate in the C-PACE Program.

C-PACE is a public-private partnership enabled by state law and financed with private capital that finances sustainability improvements such as energy efficiency and renewable energy implementation. C-PACE financing can also be used to fund portions of “green” new construction in some jurisdictions. Participating lenders (“Registered Capital Providers”) may finance these measures with long-term, fixed-rate financing, generally on a nonrecourse basis. The structure exists because the state and local municipalities view these improvements as a public benefit, akin to a sewer improvement project. Financial institutions that hold existing liens, mortgages, or security interests on commercial property must provide written consent before an interested property owner can participate in the C-PACE Program. Your institution may therefore be approached by property owners or other lenders interested in pursuing a C-PACE project. Appendix G to the C-PACE Program Guidelines (available on the program [webpage](#)) serves as a template consent document. Below is additional information for the consideration of existing lenders as well as some values of participating within the program and providing mortgage lender consent.

### Benefits of providing C-PACE consent:

- **Increased Net Operating Income (NOI)** – To be eligible for the C-PACE Program, projects must have a Savings-to-Investment ratio of at least 1 (certified by a technical reviewer). This means that the project is, in all likelihood, going to increase the NOI of the property.
- **Non-acceleration of C-PACE financing** – In the case of foreclosure, only the portion of a C-PACE assessment that is in arrears takes precedence over other mortgages or liens; the remainder transfers with the property at resale.
- **Escrow for C-PACE** – Similar to real property taxes, mortgage holders can place in escrow C-PACE financing and take control over the customer’s payment of such expenses. This can help the mortgage holder protect against delinquencies and defaults.



- **Environmental, Social, and Governance (ESG) Benefits** – Enabling a C-PACE project may allow the lender to take credit for ESG benefits provided to the customer.
- **Avoid Deployment Risk** – In the case of new development projects, C-PACE is a great tool to ensure new development projects are able to effectively fill out their capital stack. C-PACE is typically a more attractive financing tool than mezzanine debt or preferred investors and can increase the likelihood of project viability. The costs associated with reviewing a project that never comes to fruition can be significant for a primary lender. Allowing for C-PACE financing can avoid such deployment risks.
- **Customer Retention** – Property owners appreciate a smooth and efficient process for securing project financing. Facilitating this process by providing mortgage lender consent can increase the likelihood of retaining the customer relationship long term.

## SENIOR LENDERS

C-PACE lenders are limited to funding a defined list of “Energy Saving Improvements” and typically funding is limited to 35% of a property’s value. These lenders closely work with hundreds of banks, life insurance companies and other lenders throughout the country to complete the necessary capital stack (new construction/ redevelopments) or to supplement existing mortgages (retrofits). In each of these cases, senior lender must provide consent before closing. The C-PACE lender typically underwrites and closes in parallel to ensure the end financing structure meets the requirements of both lenders. C-PACE has gained widespread acceptance in the national banking community with over 280 banking institutions working alongside C-PACE lenders to date. Certain agency lenders have also approved the program and issued specific approval guidance for underwriting alongside C-PACE. These agency lenders include the U.S. Department of Agriculture, the U.S. Department of Housing and Urban Development (multifamily), the U.S. Small Business Administration’s 7(a) program, and Freddie Mac.

## UNDERWRITING

C-PACE funding creates an additional annual payment obligation for the property. Most senior lenders (and C-PACE lenders) factor C-PACE payments into their existing debt service coverage requirements. However, some senior lenders do not underwrite the C-PACE payments if they are planned to be fully passed on to tenants via triple net (NNN) leases. C-PACE is often used to reduce equity needs or to eliminate the need for mezzanine debt, preferred equity, or other expensive gap financing, but it is important to note that the Efficiency Maine C-PACE Program has loan-to-value, debt service coverage, and assessment-to-value requirements. Registered Capital Providers often have additional equity requirements and evaluate limits in concert with the senior lender to ensure both parties are comfortable with the final capital stack.



## **VALUATION**

There is general consensus among appraisers that C-PACE payments are a financing arrangement such that the payments are considered as “below the line”. The payments are not a perpetual expense as they have a limited life of 15-30 years and C-PACE is open to prepayment at any time (subject to negotiated prepayment fees).

## **ACCOUNTING**

For accounting purposes, some property owners have treated the balance of the C-PACE tax assessment as an off-balance sheet obligation (because C-PACE is an obligation of the property that could transfer on sale), while others have treated the balance as an on-balance sheet obligation. Borrowers should consult with their Certified Public Accountant to determine the appropriate C-PACE accounting treatment.

## **REPAYMENT**

Registered Capital Providers directly bill and collect C-PACE assessments as a dedicated agent of the Participating Municipality. This simplifies the repayment process, eliminating the need for separate line items on property tax bills and remittances from Participating Municipalities.

## **DEFAULT SCENARIO**

C-PACE is considered a split priority given that the financing is secured via the levying of a C-PACE assessment against the subject property. C-PACE assessments are given a priority interest on payment under foreclosure laws (with the exception of municipal liens). However, the priority only attaches to any current and/or delinquent amount due. The balance of the C-PACE assessment will always be completely subordinate to any senior debt, as it is specifically non-callable/accelerable (i.e., a “silent second” mortgage). Under a payment default scenario, the unpaid but currently due C-PACE payments plus delinquent interest and fees may be pursued. The process to collect provides a senior lender and borrower a lengthy and predictable timeline to bring the property current or to negotiate a work-out or other solution prior to a tax foreclosure sale. In the event of a foreclosure, the property would be sold free and clear, but subject to the C-PACE assessment. As the C-PACE assessment is non-callable/accelerable, any delinquent portion of the C-PACE assessment would be due and payable by the winning bidder (bank or third-party). The purchaser (bank or third party) will then be required to pay future C-PACE assessments as they come due. No consent or approval of subsequent property owners is required by the C-PACE lender or any other party. Some Registered Capital Providers have the ability and flexibility to work with senior lenders to devise collaborative workouts.



## **BANKRUPTCY**

In the event of a bankruptcy filing, the C-PACE lender would not have the same legal rights as any other creditor in relation to a C-PACE payment delinquency. The only amount that would ever have priority in front of a senior lender is the delinquent amount of the C-PACE assessment payment in arrears. The loan is non-accelerable, even in a bankruptcy. In the event of a Chapter 7 case, the C-PACE assessment would remain attached to the property and become the obligation of the new owner of the property. In the event of a Chapter 11 or 13 case, the C-PACE assessment would be required to be paid over a period as part of the repayment plan. Note that a property owner or guarantor may owe other obligations to a C-PACE lender that may be treated differently than the C-PACE assessment payment obligations of the property owner and/or guarantor in the event of a bankruptcy filing.

## **POTENTIAL STRUCTURAL RISK MITIGANTS**

- Notice and cure periods via Intercreditor Agreement
- Long process to foreclose
- Guaranty of C-PACE payments
- Full escrow of C-PACE funds with senior lender
- Payment reserve after extended Cap-I period