Capital Providers
Castle Green
CleanFund
Counterpointe SRE
Dividend Finance
Greenworks Lending
Inland Green Capital
PACE Equity
PACE Loan Group
Petros PACE Finance
Stonehill
Twain Financial

Law Firms
Bricker & Eckler
Chapman and Cutler
Hirschler
Kramer Levin
Norton Rose Fulbright
Stinson
Winston & Strawn

Program Administrator
EIC NY

Accounting Firm
Novogradac & Company

FinTech Partner
T REX

Service Provider
Citadel SPV

DETERMINING THE C-PACE FINANCING TERM & CALCULATING MATURITY DATES

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What is C-PACE?

Commercial Property Assessed Clean Energy (C-PACE) is an alternative financing mechanism for property upgrades that improve energy efficiency, utilize renewable energy, conserve water, or promote other public benefits authorized under state law. C-PACE makes it possible for for-profit or nonprofit owners of commercial, industrial, multifamily, and other property types to obtain low-cost, long-term, fixed-rate financing. Currently, 30+ states have enacted C-PACE-enabling legislation, resulting in more than $2 billion in private financing of 2,600+ projects.

How are C-PACE programs enabled?

C-PACE programs are authorized by state statute and implemented through the adoption of an ordinance or resolution by local governments. Local governments often appoint one or more third-party administrators to oversee the day-to-day operations of C-PACE programs. In addition, many local governments operate C-PACE programs directly.

What should be considered when determining the maximum allowable term of financing in C-PACE?

In determining the financing term and calculating the maturity date for a C-PACE financing, the C-PACE Alliance recommends the following principles for consideration by governments, programs, and capital providers.

C-PACE programs are authorized by states and implemented by local governments. As such, guidance on how to treat the financing of capitalized interest and other interest-only periods may be written in the state statute; a local government's ordinance or resolution; or the guidelines issued by the program administrator. This paper uses these definitions:

- **Capitalized Interest**: An amount of interest included in the C-PACE financing amount to cover the interest payments that are due. C-PACE financing is often used for adaptive reuse and new construction projects with longer periods of construction than retrofit projects. No payments are required by the property owner during a period funded by capitalized interest because the capital provider pays itself from the funds added into the principal amount for this purpose.

- **Interest-Only Period**: A period during which the capital provider agrees to allow the property owner to pay only an interest component and no principal, which aligns with commercial banking practices.

Most C-PACE programs specify the financing term cannot exceed the "weighted average expected useful life of the financed improvements" or EUL. In other words, the term of the C-PACE financing cannot be longer than the useful life of the eligible improvements being funded with the C-PACE dollars. The EUL is typically determined by an engineer or other qualified energy services professional when completing the energy analysis otherwise required by the C-PACE program.

Construction completion (or project completion, for projects that do not require construction) is generally determined as the time when an asset is placed in service. The EUL "clock" should start when construction is complete, which is generally when the C-PACE asset is placed in service. "Placed in service" is decided by the facts and circumstances that determine whether the property is in a state of

readiness to perform the function for which it is intended. Receiving a certificate of occupancy (COO) is a rule-of-thumb for determining when an asset is placed in service, but COOs can be issued before an asset is placed in service. It is also conceivable that readiness could occur before a COO.

Since property owners may not have sufficient cash flow to pay C-PACE assessments during the construction period of an asset, capital providers may offer an interest-only period during construction. Interest that accrues during a construction period can be financed as capitalized interest. The property owner and capital provider do their best to estimate the length of time an asset will be under construction, not know precisely when the project will, in fact, be finished. If the expected completion date will fall close to a tax payment date (semi-annually or annually, depending on the jurisdiction), then the EUL clock and the first assessment payment will be closely aligned. With carefully structured C-PACE financing, it is possible to exclude the construction period for an asset from the EUL. The EUL is what it is; the question is when does one start the clock running.

Capital providers may offer property owners a period of interest-only payments after completion of construction. The intent of these types of interest-only periods is to allow for revenue and expense to stabilize prior to an asset being obligated to pay principal and interest. Once the construction period is complete and the asset is placed in service, the maximum financing term is determined by EUL, and therefore cannot be further extended by inclusion of an interest-only period. In all cases the maximum financing term must be complete within the available EUL for the asset.

Any interest-only period beyond the asset's actual placed-in-service date is time that reduces the remaining EUL, and amortization of the asset may need to occur over a shorter remaining period.

How do the guiding principles apply to an example transaction?

An example may be helpful: Assume a C-PACE program has no numerical limit on the C-PACE financing term but requires that the term not exceed the EUL of the financed improvements. Further assume the transaction to be financed begins with a 24-month period of construction, and the energy analysis prepared by a third-party professional indicates an EUL for the financed improvements of 25 years. As for the financial terms of the transaction, assume the capital provider agrees to provide C-PACE financing with a 24-month construction period, followed by a 25-year term financing that begins with a 3-year interest-only period. In this case, the 25-year term would not violate any programmatic requirements because there is no numerical limit to the financing term, and the 25-year term is equal to the EUL of the financed improvements determined by the third-party professional. If the financing closed in 2000, is the appropriate maturity date in 2025, 2027, or 2030?

CORRECT INTERPRETATION:

Utilizing the principles in this paper and assuming the facts above, the appropriate maturity date would be in 2027. To sum up this example:

- with a closing in 2000,
- followed by a 24-month construction period paid by capitalized interest, where funds are reserved and no C-PACE assessment is levied against the subject property,
- followed by a 25-year EUL financing term that includes a 3-year interest-only period,
- the appropriate maturity date is in 2027.

In other words, years 2000 and 2001 would be the capitalized interest period, and the first C-PACE assessment would be levied in 2002. Years 2002, 2003, and 2004 would be the interest-only period that is correctly included in the 25-year EUL calculation, and therefore the maturity date is in 2027.

INCORRECT INTERPRETATION:
If the maturity date were set in 2025, the EUL calculation would have mistakenly included the 24-month period of capitalized interest, when no C-PACE assessments are due. A capitalized interest period up to the first assessment payment date is excluded from the EUL and therefore extends the maturity date of the financing.

INCORRECT INTERPRETATION:
If the maturity date were set in 2030, the EUL calculation would have correctly accounted for the 24-month capitalized interest period, but mistakenly extended the maturity date for the 3-year interest-only period, which is properly incorporated into the EUL financing term. An interest-only period when C-PACE assessments *are* due should be included in the calculation of the EUL financing term.

The C-PACE Alliance welcomes comments on this white paper and others available at https://www.c-pacealliance.com/what-we-do/publications/.