

CaliforniaFirst PACE Program Finances Clean Energy Projects for Commercial Property

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Property assessed clean energy (PACE) programs are an innovative mechanism for financing energy efficiency and renewable energy improvements on private property. They also present a number of challenges to investors—for one, the variance between different programs (even within a particular state) and an understanding as to how particular programs work remains an impediment to investors and to scalability. This post provides a brief overview of PACE programs generally and one particularly popular PACE program – CaliforniaFirst.

Overview of PACE

PACE programs vary by state, but most allow property owners to finance clean energy projects through a voluntary property assessment paid as a line item on their property tax bills. Thirty-two states and the District of Columbia have enacted PACE-enabling legislation and there are active PACE programs in 19 states and the District of Columbia. While most of these states provide financing for commercial PACE projects, only California, Missouri and Florida have active residential PACE programs.

CaliforniaFirst PACE Program for Commercial Property

The CaliforniaFirst PACE program is one of 12 PACE programs active in California and is available for both residential and commercial real property. CaliforniaFIRST is offered by the California Statewide Communities Development Authority (CSCDA) and is currently available in more than 40 California counties, with over 330 participating local governments.

Using the CaliforniaFirst PACE program (Program), commercial property owners can work directly with a clean energy developer and the CSCDA. The developer agrees to install the clean energy project and provide power to the property owner through a power purchase agreement or lease. The property owner pays for the project through a contractual assessment, which appears as a line-item on the property tax bill.

The CSCDA secures the payments through a notice of assessment recorded on the property title. The contractual assessments have priority over any existing mortgage lien. If the property owner

sells the property, the repayment obligation remains an obligation of the property. The Program's underwriting criteria focuses primarily on the relevant payment history and value of the property. The clean energy project must have an effective useful life of at least five years and only new systems can be financed through the Program. The Program is administered by a third-party administrator (Renewable Funding LLC).

As an "interim financing mechanism," CSCDA and a clean energy developer would typically enter into an assignment and assumption agreement under which CSCDA assigns its rights to receive the contractual assessments to the clean energy developer in exchange for the clean energy developer assuming CSCDA's financing obligations under the assessment contracts, plus certain specified costs. The assignment term is expected to last three years. On or prior to the end of the assignment term, CSCDA issues bonds to the clean energy developer in exchange for the property tax assessments that were assigned to the clean energy developer. The principal amount, maturity date, amortization and interest rates of the bonds are designed, in the aggregate, to produce cash flows that replicate the principal and interest components of the contractual assessment installments.

From an investor point of view, PACE payments are a senior benefit assessment lien on the property, and a new owner of the property would inherit the solar PV benefits and the PPA/lease payment obligation through the PACE program. In the event of a default, the remedies are fairly strong—for instance, CSCDA has the right to have the delinquent installment and its associated penalties and interest removed from the secured property tax roll and immediately enforced through a judicial foreclosure action. In the event of foreclosure, the proceeds of the foreclosure sale would be used to pay any delinquent amounts and future installments would become the responsibility of the purchaser.

Considerations for Investors

By statute, the owner of the renewable energy improvement is not permitted to remove the improvement from the property prior to the end of the assessment term. Investors should be aware that in the event of payment default they will not have the ability to seize the improvement and will need to rely on the public agency to foreclose on the property. Additionally, the public agency in charge of the PACE program is a third party beneficiary with respect to the power purchase agreement or lease until the assessment lien is fully repaid and also has consent rights over any amendments to the customer agreement. Therefore, it may be difficult for a developer or financing entity to revise a power purchase agreement or lease once it is in place.

Conclusion

PACE programs are likely to attract more investors and commercial property owners as they become more widely available and clean energy developers become more experienced working with them. We've highlighted the basics of the CaliforniaFirst program for commercial property, but investors, property owners and developers should ensure that they understand the regulatory nuances of the particular program in their area.

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