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PENNSYLVANIA'S PACE PROGRAM IS OPEN FOR BUSINESS

BY MATT MAHONEY, MARK HIMMEL, AND DAVE ZEHALA

Introduction: Property Assessed Clean Energy (PACE)

PACE is a proven financing mechanism that provides owners of large buildings with a flexible, user-friendly tool for maintaining and improving their property's energy and water infrastructure. According to the Department of Energy's Better Building Initiative, the top two roadblocks that property owners face when addressing these systems are not having the funding to pay for these projects and the long payback period. PACE eliminates these barriers by offering a financing solution that preserves owners' equity while keeping tenants comfortable and happy.

When property owners are budgeting an energy and/or water project, they're using PACE to finance the design, materials, and labor for the elevators, lighting, controls, air handlers, and other infrastructure because PACE safeguards equity and stabilizes cash flow during and after construction. The same benefits apply to retrofit, gut-rehabilitation, rebuild, and everything else on the spectrum. Now, PACE is open for business in Pennsylvania and lawmakers incorporated best practices from other PACE states to offer a flexible, owner-friendly program that meets the diverse needs of Pennsylvania's building owners.

Pennsylvania PACE: Setting the Scene

In June of 2018, Governor Wolf signed Senate Bill 234 into law, amending Title 12 (Commerce and Trade) of Pennsylvania's Consolidated Statutes to add Chapter 43, a Property Assessed Clean Energy Program, or PACE. The bipartisan support of Pennsylvania's legislature, along with Governor Wolf's signature, enabled local governments across Pennsylvania to establish PACE Districts to, "ensure owners of agricultural, commercial and industrial properties can obtain low-cost, long-term financing for energy efficiency, water conservation and renewable energy projects."

PACE may be new to Pennsylvania, but it's not new in real estate markets across the nation. According to PACENation, a national nonprofit that advocates for PACE financing, PACE is active in 22 states plus D.C. where thousands of projects have invested over a billion dollars in properties across the U.S. In nearby Columbus, OH, $100 million has been invested with PACE, boasting the largest concentration of PACE financing of any region in the country.

PACE financing is widely recognized as a game changer in the commercial real estate community. Commercial property experts see PACE as a financing program that removes many of the hurdles faced when addressing a property's energy and water infrastructure. Local governments see PACE as a job creator and economic development tool. But what is PACE and how does it work?

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What is PACE Financing?

PACE is a public-private partnership between local governments and commercial-scale property owners. In this partnership, a private owner agrees to voluntarily place a special assessment on their property. In return, the property owner can access up to 100 percent of the financing for improvements to their property's energy and water systems at a fixed rate over a term lasting up to 30 years. The government entity then enforces and collects the special assessment as they would a typical real estate tax, and passes the PACE payments through to the capital provider.

PACE effectively leverages the same system used to improve public infrastructure with private property owners, such as sewage or water assessments. The local government issues a special assessment to a property owner that needs to improve the infrastructure serving their property which also benefits the public.

PACE Eligible Investments

PACE can be used to finance the energy and water infrastructure needs of a ground up construction to a retrofit of an existing building and everything in between. PACE financing funds projects that demonstrate a savings to investment (SIR) ratio greater than 1, meaning the PACE financed improvement should be cash flow positive and self-finance through the savings created.

One misconception is that PACE-financed improvements must conform to a specific performance standard, such as the US Green Building Council's LEED Standard or the Department of Energy's EnergyStar standard. While projects that are LEED- or EnergyStar-certified qualify for PACE, the certifications are not a prerequisite for the financing. PACE supports public policy goals designed to drive higher efficiency, however, PACE is more often used to replace an aging boiler that is nearing the end of its useful life. If a new boiler is more efficient than an old boiler, it can qualify for PACE. Taking it one step further, if that boiler requires a new pipe or piece of supportive infrastructure, that qualifies, too. In fact, all of the design costs, underwriting, and other soft costs are financeable through PACE, often providing owners 18-to-24 months until the first PACE payments are due.

Pennsylvania PACE Restrictions

There are restrictions to Pennsylvania's PACE program. Multifamily and residential properties are currently prohibited from using PACE. Also, government owned properties cannot use PACE because the government entities establishing PACE programs are the same entities collecting and disbursing PACE payments. Fortunately, government entities have access to Pennsylvania's Guaranteed Energy Savings Program which replicates many of the same benefits as PACE.

Additionally, because PACE is special assessment and not a conventional loan, the PACE capital provider cannot accelerate if the property owner faces financial hardship. If an owner is facing foreclosure, PACE capital providers must wait through the same process as the government when seeking unpaid taxes.

Pennsylvania PACE Requirements

When compared to other debt financing, PACE only has a few additional requirements. First, PACE requires a professional engineering report to determine baseline energy use and to verify energy/water savings. This report, when completed properly, provides property owners with information that will help maximize resource allocation and provides assurance to the private PACE underwriters that the investment is sound and secure. Second, PACE requires written consent from existing lenders on the property. This is required because PACE is treated as a tax, and therefore has the same priority level as a tax. Currently, there are hundreds of capital providers across the U.S. that have consented to authorizing PACE financing on a property where they have a lien. Third, PACE assessments must be recorded on the property's title so PACE payments can be transferred to a new owner when ownership changes.

PACE Benefits

Aside from the benefits of financing a capital improvement project over its estimated useful life with zero capital outlay, PACE has other benefits that are built into the program, including:

1. PACE is a tax and can be recorded on an income statement instead of the balance sheet.

2. PACE can be included as a CAM charge under certain lease structures.

3. Pennsylvania PACE financing is available from a variety of sources.

4. Pennsylvania PACE can refinance qualified projects.

5. PACE works hand-in-hand with tax incentive and rebate programs.

The PACE Process

The PACE process can be broken down into four easy steps.

Step 1 – PACE Assessment: Hire a professional to conduct an engineering audit to identify a portfolio of eligible energy projects and establish energy/water baselines.

Step 2 – PACE Financing and Compliance: obtain lender consent and authorization from the county

Step 3 – Design and Build: PACE disburses directly to construction partners based on project progress and property owner decisions

Step 4 – Measure and Verify: work with a contractor or self-perform in some cases to verify energy savings

Summary

PACE gives commercial-scale owners a better choice for financing energy and water savings projects, allowing owners and tenants to realize benefits immediately. Commercial real estate markets across the U.S. have been leveraging PACE to finance projects that self-fund from the utility, operations and maintenance savings they create. PACE is shifting the budgeting conversation from seeking a better ROI to immediately improving NOI, all while strengthening equity partners' positions and configuring operational line items to ensure owners share the benefits of their investment with their tenants. BG

Matt Mahoney is a senior project developer for Plug Smart. He can be reached at matt.mahoney@plugsmart.com. Dave Zehala is president of Plug Smart. He can be reached at dave.zehala@plugsmart.com. Mark Himmel is director of project development for Plug Smart. He can be reached at mark.himmel@plugsmart.com.