

PROPERTY MANAGEMENT

Quarterly

FINANCE

Colorado C-PACE responds to challenging market

Commercial Property Assessed Clean Energy financing enables owners of eligible existing commercial and industrial buildings to finance up to 100% of the costs related to energy efficiency, renewable energy, water conservation and resiliency improvements. Financing is provided by private capital providers at competitive rates, with repayment terms up to 25 years. The program can also finance a portion (15%-35%) of development costs associated with new construction projects (copace.com).

■ Challenging market conditions. On March 16, 2022, the U.S. Federal Reserve began one of the most aggressive interest rate hiking efforts in history. As a result, interest rates are now at a 22-year high. This high interest rate environment coupled with continuing challenges stemming from the COVID-19 pandemic have led to:

- High vacancy rates;
- Declining property valuations;
- Supply chain constraints;
- Construction material cost volatility;
- Labor availability constraints;
- Stricter lender underwriting requirements;
- Regional bank failures; and
- Heightened concerns of commercial real estate loan portfolio risk.

Given these challenges, it is not surprising that building owners across Colorado are struggling to retain tenants, mitigate declining revenue growth and manage increased expenses (contract services, utilities, insurance, maintenance and repairs, payroll, etc.) while at the same time meet new building energy performance standards.



Tracy Phillips
Program director,
Colorado C-PACE

■ Colorado C-PACE program changes.

In response to these unprecedented market challenges, the Colorado Energy Office, with support from Sustainable Real Estate Solutions' C-PACE Program Administration Team, spearheaded legislative efforts to improve

and expand Colorado C-PACE. These exciting new legislative changes went into effect Aug. 7.

In addition, the Colorado New Energy Improvement District board also approved three strategic program updates that will make the benefits of C-PACE financing more accessible to a broader range of projects. These forward-looking program updates will provide property owners, developers, and lenders with a valuable tool to help navigate today's challenging market environment.

■ Eligibility of resiliency improvements. As part of the legislative changes, resiliency improvements are now eligible for financing through Colorado C-PACE. These are improvements that increase a building's resiliency and includes improvements that:

- Increase a building's structural resiliency for seismic events;
- Improve indoor air quality;
- Improve wind or fire resistance;
- Improve stormwater quality or reduce on-/off-site risk of flash flooding;
- Improve the ability of a building to withstand an electrical outage; and
- Reduce/mitigate urban heat

island effect or the effects of extreme heat.

■ Financing process efficiency improvements. The new legislation also introduced several process efficiency changes that:

- Eliminate the requirement for a 30-day comment period between the completion of lender underwriting efforts and finance closing;
- Eliminate the requirement for public hearing; and
- Eliminate the requirement for a \$1,000 deposit to initiate the finance closing process.

These process efficiency improvements will provide transaction parties with increased flexibility and accelerate the C-PACE finance closing process.

■ Retroactive project financing: Longer lookback period and inclusion of retrofits. Retroactive project financing enables an eligible property owner that has recently completed a new construction or gut rehabilitation project to refinance these projects via Colorado C-PACE. The NEID board recently approved an increase to the lookback period for retroactively financed projects from two years to three years.

Furthermore, retroactive financing has been expanded to support existing building retrofits, in addition to new construction and gut rehab projects. Retroactively financed improvements on existing buildings must be part of additional (new) retrofit improvements planned to be financed through the C-PACE program and represent no more than 35% of the total project finance amount.

■ New construction project finance amount expansion. C-PACE financing for new construction is commonly used to replace more expensive sources of capital (e.g., mezzanine debt, or as a "gap filler") to help

developers build their capital stack and improve the economic viability of their projects.

In the current difficult lending environment, project developers are facing significant challenges securing economically attractive financing terms for their high-performance new construction designs. To better serve efficient and sustainable new construction designs, Colorado C-PACE has expanded its maximum eligible lending amounts. Projects with designs that exceed the 2018 International Energy Conservation Code by at least 5% in terms of energy performance can now receive up to 30% (increased from 20%) of their total eligible construction costs through C-PACE. Projects that meet or exceed the 2021 IECC can receive up to 35% of their total eligible construction costs through C-PACE. (Projects that meet the 2018 IECC are still eligible for 15% of their total eligible construction costs through C-PACE).

■ Conclusions. These program changes will help Colorado C-PACE participants meet the challenges in today's difficult market environment. Moreover, these upgrades will make the program more inclusive of all Colorado communities, developers and building owners and build on the program's foundation of success:

- \$250 million in financing for over 120 projects;
- 52 C-PACE lenders – a level of capital provider diversity and participation unmatched in the industry; and
- 39 participating counties – representing 96% of the state's commercial building stock, including urban, suburban and rural communities. ▲

tphillips@copace.com