

C-PACE primer for mortgage lenders

Commercial Property Assessed Clean Energy (C-PACE) Real Estate Finance Product



Background

C-PACE is a public-private partnership enabled by state law and financed with private capital that finances sustainability improvements to CRE such as: energy efficiency, water conservation, seismic resiliency and wildfire hardening. C-PACE financing can also be used to fund portions of “green” new construction in some jurisdictions.

Nuveen Green Capital finances these measures with long-term, fixed-rate financing, generally on a non-recourse basis. The structure exists because the state and local municipalities view these improvements as a public benefit, akin to how a sewer improvement would benefit the public.



Where Nuveen Green Capital Lend:

AK, CA, CO, CT, DE, FL, HI, IL, KY, MA, MD, ME, MI, MN, MO, MT, NE, NJ, NM, NV, NY, OH, OK, OR, PA, RI, TN, TX, UT, VA, WA, WI & D.C.

SENIOR LENDERS

C-PACE lenders are limited to funding a defined list of “eligible improvements” and typically funding is limited to ~20-30% of a property’s value. As a result, we work very closely 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, we need the senior lender’s consent before closing and typically underwrite and close in parallel to ensure the end financing structure meets the requirements of both lenders.

C-PACE has gained widespread acceptance in the 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 USDA, HUD (multifamily), SBA 7a, and Freddie Mac. Fannie Mae, SBA 504, and HUD Multifamily (new construction only) have not yet consented to C-PACE.

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 NNN leases. Most of Nuveen Green Capital's financings are underwritten to a combined 1.25x DSCR although exceptions are sometimes made for properties in central business districts of top MSA's.

C-PACE is often used to reduce LP equity needs or to eliminate the need for mezzanine debt, preferred equity, or other expensive gap financing, but it is important to note that Nuveen Green Capital has LTV, LTC and equity requirements with limits on an overall project leverage and minimum owner equity. Nuveen Green Capital evaluates these 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 CPA to determine the appropriate C-PACE accounting treatment.

REPAYMENT

Most C-PACE assessments are invoiced as a line item on the property's existing property tax bill and are paid directly to the applicable tax assessor, who then remits funds to Nuveen Green Capital. Specific mechanics vary by jurisdiction and a minority of C-PACE programs have payments made directly to Nuveen Green Capital, a 3rd party servicer, the C-PACE program administrator, or a governmental entity.

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. 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 a 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.

Nuveen Green Capital is a balance sheet lender and handles its servicing in-house. One of the benefits of working with Nuveen Green Capital is that Nuveen Green Capital has 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

ABOUT NUVEEN GREEN CAPITAL

Nuveen Green Capital is a national leader in sustainable commercial real estate financing solutions and an affiliate of Nuveen, the investment manager of TIAA responsible for \$1T+ in assets under management as of February 27th, 2023. Established in 2015 by the C-PACE industry's founders and standard-setters, Nuveen Green Capital is a private capital provider dedicated to making sustainability a smart financial decision for commercial real estate owners who seek to improve the energy, water and resiliency performance of their property. For more information, visit www.nuveen.com/greencapital.