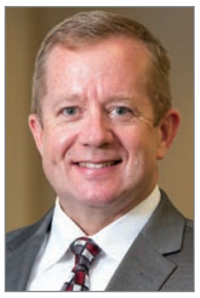
Lending

1st CO multifamily project capitalizes on C-PACE



Eric V. Snyder, Esq.
Attorney, Moye White LLP

Although articles have been written about the financial benefits of Commercial Property Assessed Clean Energy program, many real estate developers, brokers and lenders are still not aware of the availability of its low-interest, long-term, nonrecourse financing for most energy conservation, renewable energy and water conservation aspects of real estate projects.

Colorado's C-PACE program is a newer financing tool available for commercial property owners to help bridge the gap in financing available from traditional commercial loans and other capital sources. Under the C-PACE program, the New Energy Improvement District was created as a mechanism to provide additional capital for portions of commercial properties. Property owners who voluntarily allow a new property tax assessment from the NEID (in the amount of financing from a third-party lender) can tap into the available capital on terms not otherwise available from traditional lenders. The assessment is then repaid via property tax payments to the county treasurer, who remits payment to the NEID. The NEID, in turn, makes the required repayments to the capital provider.

Almost every developer and property owner who has utilized C-PACE financing for commercial properties have done so for capital improvements to existing buildings. Those buildings typically are in dire need of a remedy to offset the increasingly high utility costs. Most owners obtain a new roof; insulation; heating, ventilation and air-conditioning; and new windows or window treatments.

Utilizing PACE financing for residential properties (known as R-PACE) is not yet available in Colorado. The enabling statutes provide that PACE financing shall be available for any "eligible real property," which includes both residential and commercial buildings, but the Colorado program has not yet implemented R-PACE financing for residential properties in Colorado due to consumer protection concerns.

However, what many developers may not know is C-PACE financing is available for multifamily properties so long as there are five or more units in the development. To date, only one project in Colorado has utilized the C-PACE financing for a multifamily property: 1515 Flats apartments in the Sloan's Lake area located at 1515 Vrain St. in Denver. Not only is this the first Colorado C-PACE multifamily project, it also is the first project in the entire country to implement C-PACE financing on new construction rather than as a retrofit to an existing building.

A misnomer about C-PACE financing is that after the energy conservation, renewable energy and/or water conservation improvements are made, the building must be especially "green" to qualify. In addition, unlike C-PACE programs in other states, Colorado does not require the energy-efficiency, renewable energy and water conservation measures to entirely offset the higher tax burden. Under the Colorado C-PACE guidelines, the buildings need only to perform more efficiently than the average of their asset class. After the city of Denver adopted the 2015 International Energy Conservation Code, all new construction projects in Denver should qualify. New buildings should easily outperform the average of other older buildings that were not designed and built with higher energy-efficiency standards.

So, what does this mean for developers and property owners?

A significant portion of the capital costs for construction may be obtained via the C-PACE financing assessment with the NEID, rather than a larger share of the capital costs coming from typical commercial loans or additional cash from the developers or investors. Most commercial loans are relatively short-term (between five and 10 years), are recourse to the borrower, must be satisfied upon a sale of the property and may only be used for hard costs. The C-PACE financing allows for up to a 20-year repayment period, is nonrecourse to the borrower, may be used for both hard and soft costs, and need not be paid in full or satisfied upon a sale of the property. When the property is sold, the NEID assessment remains and is the sole obligation of the new owner.

The 1515 Flats project is a mixed-use development that contains commercial use on the ground floor with 82 multifamily units above and is near completion. The project includes higher energy-efficient roof, walls and windows, a dedicated outdoor air system, fan coil unit heating and cooling system, domestic hot water, LED lights and roof-mounted solar PV panels. The developers Leon Cisneros and Courtney McRickard with their companies utilized PACE Equity to provide the expertise and project financing. Approximately $2.8 million of the project financing was obtained through the C-PACE program, which represented 16 percent of the total development. Usually, the C-PACE financing cannot exceed 15 percent of the total development, but because PACE Equity and the developers were able to obtain a 56.1 percent reduction of energy over the local building code requirements, they were able to increase the amount of funding through C-PACE.

Another incentive for C-PACE financing is the ability to eliminate the split-incentive issues that face most commercial property owners. Landlords are not inclined to make significant capital improvement expenditures without some incentive and a possible return on investment. Until now, spending scarce capital for a new roof, insulation and window treatment was not feasible or economically viable. With C-PACE, since the financing repayment is made via property tax payments to repay the NEID assessments, savvy property owners can recover the amounts of the NEID

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in Lakewood, Golden, West Colfax and South Pearl Street started to decline in favor of the auto. With dominance of the auto came decentralization of land uses. Since there are few choices for transportation other than the auto, when suburban development occurs, there's a readily apparent impact on traffic and a possible degrading of the 15-minute community.

The challenge facing developers and residents is how to maintain the communities that we've created or bought into in the face of seemingly rampant construction, quickly worsening traffic and a sometimes-frightening change of landscape, populated by more building and people. Depending on one's perspective, this could be exciting or scary. For pro-development urbanists, development means more choices in their 15-minute community. For the anti-development skeptics, new building threatens their 15-minute community.

Is development necessarily antithetical to the goals of those skeptical to development? I don't believe so, and we can point to a set of great projects that started with – and were improved due to – years-long discussions with neighbors. Our (mostly) successful history of working closely with neighborhoods is manifested in projects like RiverClay Condos in Jefferson Park and Coda in Cherry Creek where discussions with neighbors recognized and owned potential traffic and height impacts. Addressing these is a matter of bearing witness to our projects' impact. I always start neighborhood meetings with the recognition that "I'm an uninvited guest into your neighborhood," that they know more about their neighborhood than I do and that I find if I listen, the resulting projects are better.

Rather than obfuscate, we share traffic studies – going so far as undertaking studies when not required – in recognition of impacts, shade studies and vehicular access plans. In Boulder, we're intently focused on neighborhood flood concerns. In Denver, we hope to address a neighborhood's sense of loss of affordable housing by building mixed-income communities. After we won a city of Denver-issued request for proposal for the redevelopment of a surplus land parcel in Jefferson Park, I asked Glenn Harper, the neighborhood president, why we received the neighborhood's support in the selection among 10 responding developers. His response was clarifying and, in many ways, simplifying: Zocalo was the only developer to have asked the neighbors what they wanted to see built.

In Cherry Creek, a similar emphasis on neighborhood goals focused us on lessening traffic impacts. In working with the Cherry Creek North Neighborhood Association and providing financial support to its transportation nonprofit, Transportation Solutions, we crafted traffic-mitigating strategies that provided options to our future residents at Coda and to the neighborhood at large. Current Denver City Councilman Wayne New, then the neighborhood association's president, moved from skeptic to supporter after Zocalo delivered on the development of Coda and on our commitments to the neighborhood.

Do these steps guarantee no impact? Of course not. But what they may ensure is that the development is responsive to certain top-line issues of neighbors. These issues will be those – whether in the suburbs or in cities – that help to strengthen the 15-minute community.

Real estate development and, in particular, residential development, is increasingly difficult. Threading the needle may be an apt metaphor. Though the broader good in attempting to stitch together projects that also deliver on community goals is powerful and will lead to stronger, healthier communities.▲

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assessments from tenants so long as the leases provide for the tenants to pay for such costs. It is a win-win situation for both landlord and tenants. The landlord has a much more viable, long-term sustainable asset, while the tenants have lower overall costs when the utility cost savings are taken into effect.

The vast majority of projects that have implemented the energy conservation, renewable energy and water conservation aspects with C-PACE financing have more than paid for the higher tax costs, to the point where they are realizing significantly higher returns on investment. Not only can developers and property owners now build better, more sustainable buildings and reduce energy consumption, they also can improve the bottom line with C-PACE financing.▲

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of lending options and familiarity working with organizations like LIFT, which aims to end the cycle of poverty for families in Chicago, Los Angeles, New York and Washington, D.C., and Community Solutions, which supports more than 75 communities nationwide in their mission to end homelessness.

The team was able to underwrite Arroyo Village's social services component and structure the deal with protections for all three important parties (developers, investors and residents) – with a roomier budget.

The deal moved to completion, and Arroyo Village broke ground in September. It's on the path to delivering vital community services while epitomizing social change through real estate.

"Arroyo Village means that 130 households will have access to safe, dignified, truly affordable housing," said Curtis. "We are preserving and increasing low-income housing stock in a neighborhood that is quickly gentrifying and, in the process, creating a true village."

This transaction shows that with creativity and determination, lenders can finance projects that meet deep and difficult community needs, ensure sound underwriting, and meet the needs of investors and developers. Let's make this a model for similar projects in Colorado and around the country.▲