CPACE WORKS.

MD ENERGY ADVISORS

In 1971, Alka-Seltzer®, the 2 white tablet packet that helps relieve heartburn, acid indigestion, sour stomach and pain, launched a commercial set in a neighborhood bistro where a waiter persuaded a man to sample a new dish. The actor explains: "*Came to this little place. Waiter says, 'Try this, you'll like it.' What's this? 'Try it, you'll like it.' But what is it? 'Try it, you'll like it.' So, I tried it. Thought I was going to die. Took two Alka-Seltzer.*" The actor concludes the spot by declaring: "*Alka-Seltzer works. Try it, you'll like it.*" For those that haven't seen the commercial it is a must watch and I have included a link to the right. The commercial was so iconic that it was remade in 2006 starring Kathy Griffin.

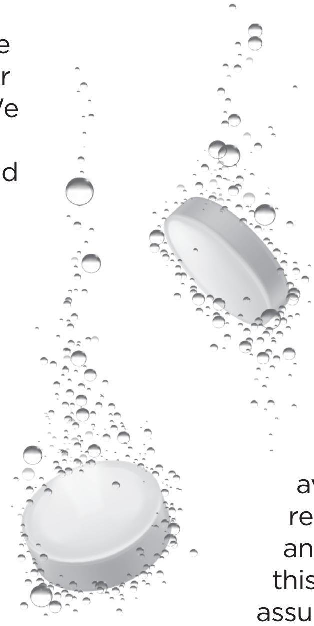
In 2001, the idea and general structure for Commercial Property Assessed Clean Energy or "CPACE" was born. In 2008, with funding from the Environmental Protection Agency, the program began to gain its footing and started to grow in popularity in 2015.

When CPACE first came onto the scene many bankers experienced heartburn similar to the main character in the Alka-Seltzer commercial as "waiters" were promoting an unknown "dish" without giving it a proper explanation. At that time, the majority of deals were cost constrained, as a result of the low interest rate environment, and not debt constrained, and CPACE was viewed as an opportunity to add additional leverage to a real estate transaction reducing the sponsor's equity requirement and improving project returns. As you can imagine, this application was like cilantro to bankers – they either loved it or they hated it!

Given today's higher interest rates, and in turn, a reduction in project cash flow, the proverbial tables have turned, and a greater number of projects are currently debt constrained rather than cost constrained. In the dynamic world that we live in, options are always a plus. CPACE fits in the capital stack regardless of market conditions – debt constraints or not – the only change is the output to sponsors/investors. Even with debt constraints, we are closing projects in all asset classes with recent successes in multifamily, office and senior housing, hospitality, and self-storage, as a result of CPACE.

Commercial Property Assessed Clean Energy (CPACE) is an innovative financing tool that makes it possible for owners of commercial, industrial and other non-residential properties to obtain low-cost, long-term financing for energy efficiency, water conservation and renewable energy projects.

In this article, we are going to play the role of a seasoned server and provide a proper explanation of the CPACE 'ingredients.' We will explain the use cases in the current market so that you, the banker, understand the ingredients and can decide what to order (we recommend trying the CPACE sandwich with a side of fries).



Just as Alka-Seltzer can be used to relieve many symptoms, CPACE is a versatile product; applications include ground-up construction, repositions/value-adds, energy-related capital projects and retroactivity for eligible completed projects. CPACE loans have fixed rates and maturities of up to 30 years, and they are repaid through an incremental property-tax assessment that remains with the asset even after a sale.

The source of repayment for CPACE loans, an incremental property-tax assessment, has caused some heartburn in the banking community since delinquent property taxes are given a priority interest under foreclosure laws. However, in the case of CPACE, the priority only attaches to any current and/or delinquent amount due. In other words, the only portion of the CPACE that can "prime the mortgage" is the annual payment of the CPACE and not the full CPACE loan amount. The balance of the CPACE assessment will always be completely subordinate to any senior debt, as it cannot be called and/or accelerated (*i.e.*, a "silent second" mortgage).

Rest assured, just as Alka-Seltzer can be used to treat many symptoms, CPACE is equally dynamic and its varied utilization is driven by market conditions.

Furthermore, the annual payment is typically capitalized in the CPACE loan until the project reaches stabilization and the project cash flow can support the CPACE payment.

Historically, CPACE minimizes a sponsor's need for costly preferred equity and/or mezzanine financing by providing additional project leverage and reducing the sponsor's equity requirement for cost constrained ground up construction and value add projects. This application of CPACE reduced the sponsor's weighted average cost of capital and increased project returns, but, as interest rates have increased and debt service coverage has decreased, this application has proved more difficult. Rest assured, just as Alka-Seltzer can be used to treat many symptoms, CPACE is equally dynamic and its varied utilization is driven by market conditions.

In 2006, Alka-Seltzer updated the *Try It! You'll Like It* commercial to make it relevant for the current times, broaden the audience and increase sell through. The new version was faithful to its predecessor, featuring small tweaks like replacing the setting from a neighborhood bistro to a chic restaurant; changing the messenger from a journeyman actor to a contemporary comedian (Kathy Griffin); and updating the original message as to why consumers use Alka-Seltzer from a remedy for ailments like acid indigestion and headache to relief for overindulgence.

– continued –

For more information, visit **www.mdenergyadvisors.com**. To talk to an energy advisor, call us at **410.777.8144**.

In 2023, we must update the use cases for CPACE to make it relevant for the current times, broaden the audience, and increase sell through. The new version is faithful to its predecessor. Use cases include applications that help with new deals, troubled deals, and reducing operating expenses while remaining compliant with energy regulations.

INTRODUCING CPACE *PARTICIPATION, PAY-DOWN AND PROJECT.*

CPACE VERSATLITY

Fixed Rate, Long Term, Non-Recourse, Non-Dilutive Source of Capital

PARTICIPATION (new deals):

Bankers still need to close deals in the current environment. CPACE lenders are actively lending in the current market, oftentimes at rates on par with senior lenders. If a bank is constrained by a loan to one borrower, size of the loan amount, or is just looking to lay off a piece of the deal, CPACE can remove the need for participation, and its associated risks, for a ground-up or conversion project by allowing a one-bank close.

PAYDOWN (troubled deals):

Recently completed projects have been slower to stabilize and delinquencies are expected to increase. CPACE can provide principal curtailment to a senior lender for a project completed in the last 36 months thereby freeing up balance sheet and replenishing interest and operating reserves.

PROJECT FINANCING (Capital Expenditure, OPEX reduction and energy compliance):

Energy-related equipment eventually breaks down and needs to be modernized. More efficient equipment will help reduce energy-related operating expenses. Additionally, many jurisdictions are adopting Building Energy Performance Standards (BEPs) like New York's Local Law 97, Washington DC's BEPs program, or Maryland's Climate Solutions Now Act. With terms as long as 30 years, CPACE loans are cash flow positive and can be utilized to fund energy-related projects such as an HVAC replacement or elevator upgrade, without the need to refinance a first mortgage or pay out of cash.

In the early 2000's, Alka-Seltzer had a nice flat business. After updating the *Try It! You'll Like It* commercial to make it relevant for the current times and broadening the audience, Alka-Seltzer increased sales by 12%!

In the early 2020's banks still need to maintain and grow their businesses. If the CPACE participation, paydown, and project financing applications are properly leveraged, CPACE can help achieve similar results to Alka-Seltzer's and can help you and your fellow bankers retain clients, decrease delinquencies, and close more transactions.

Now that you know the 'ingredients', we are confident that you will agree:
CPACE Works. *"Try it! You'll Like it!"*

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For more information, visit **www.mdenergyadvisors.com**.
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