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New Resistance Imperils the Future of PACE Financing for Clean Energy

Property Assessed Clean Energy (“PACE”) financing has been widely touted as an innovative program that can provide easily-accessed financing for millions of homeowners and businesses to make clean energy investments like installing solar panels or energy-efficiency upgrades. While still geographically limited to areas with strong incentive programs or relatively high energy prices, these programs offer easy access to money for making what can be a large initial investment. But in order for these PACE programs to continue, two evolving issues must first be resolved: (1) the debt and credit rating concerns raised by some local governments; and (2) concerns from mortgage holders about dilution of mortgage security interests by PACE assessments.

Under PACE programs, local governments use their bonding authority to raise funds, which the local governments may then “lend” to public entities, private organizations or individuals in the local community to finance specifically identified types of clean energy and energy efficiency projects. The recipients, or “borrowers”, repay the proceeds through additional assessments on the property taxes for the property improved by the clean energy or efficiency investment. By taking banks and other traditional lenders out of the lending process, funding could be streamlined to support specific types of investments, without spreading the cost over the larger community, as only the owner of that particular property is responsible for the increased property tax payment.

Initial reaction to the programs, piloted in Berkley, CA and Boulder, CO has been very positive. The Obama administration has approved of PACE with \$100 million in stimulus funding. Several states have embraced the program passing laws authorizing the use of local bonding authority to support PACE programs.

Among the many states authorizing PACE bonding was Virginia, however Arlington County, perhaps the most progressive community in the state, has yet to pass an ordinance to create a local version of the program. The County released a statement announcing “Arlington is unlikely to float its own bonds for this, as the County is facing its self-imposed debt ceiling to maintain the coveted Triple-A bond rating.” The PACE program would impose a significant administrative burden to the County. “For PACE financing to work,” the statement read, “realtors, mortgage lenders, and mortgage underwriters would need to be comfortable with its application in the housing market.”

Echoing some of the concerns raised by Arlington, mortgage holders are worried about the lien priority against PACE obligations. Standard government tax assessments—ones that are used to fund public projects—typically have senior lien priority over mortgages. As it currently stands, the property tax obligation from PACE assessments are senior to existing first mortgages. Mortgage lenders are concerned that loans secured by mortgages that could be primed by liens related to PACE assessments will not be readily sellable in the secondary mortgage market. Proponents of PACE argue that if mortgage lenders become comfortable with the concept that a PACE assessment is similar to a traditional tax assessment, it would be easier to accept the inclusion of PACE assessments as part of those assessments.

Existing and new PACE programs are awaiting a fair and equitable resolution of these issues. “If this doesn’t get resolved, PACE is dead,” said Adam Browning, director of California advocacy group Vote Solar. The state of Maine has proposed a compromise that would make PACE assessments junior to existing debt. Proponents of PACE argue that the loans must be paid before mortgages to allow local governments to raise funds for the program. But critics respond that the programs don’t do enough to ensure that borrowers are able to pay back their loans, creating severe administrative burdens for local counties and additional problems for mortgage underwriters.

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