

**REPORT REQUIRED BY TEXAS LOCAL GOVERNMENT CODE SECTION 399.009
FOR PROPOSED CITY OF CARROLLTON, TEXAS
PROPERTY ASSESSED CLEAN ENERGY (PACE) PROGRAM**

This Report is adopted by the City Council for the City of Carrollton, Texas Property Assessed Clean Energy (“PACE”) Program (the “**Carrollton PACE Program**”) in accordance with the requirements of the Property Assessed Clean Energy Act (the “**PACE Act**”) as set forth in Texas Local Government Code Chapter 399. The PACE Act was enacted in 2013.

The City of Carrollton (“City”) and its constituents benefit when older existing buildings are modified with new technology and equipment that increases energy efficiency and reduces water consumption. As described in this Report, the City is establishing the Carrollton PACE Program to encourage private sector investment in energy efficiency and water conservation. The Carrollton PACE Program will be offered to property owners on a strictly voluntary basis and will not use any public funds or resources.

As authorized under the PACE Act, the PACE program is an innovative financing program that enables private sector owners of privately owned commercial, industrial, and multi-family residential properties with five or more dwelling units to obtain low-cost, long-term loans to pay for water conservation, energy-efficiency improvements, and renewable energy retrofits. PACE loans provide up to 100% financing of all project costs, with little or no up-front out-of-pocket cost to the owner. The 2015 legislative session streamlined the process.

Loans made under the PACE Program will be secured by assessments on the property that are voluntarily imposed by the owner. Assessments may be amortized over the projected life of the improvements. The annual utility cost savings derived from improvements financed with PACE loans are expected to exceed the amount of the annual assessment payments. In turn, these improvements are able to generate positive cash flow upon installation because the debt service will be less than the savings.

PACE assessments are tied to the property and follow title from one owner to the next. Each owner is responsible only for payment of the assessments accruing during its period of ownership. When the property is sold, the payment obligation for the remaining balance of the assessment transfers automatically to the next owner. As a result, the program will help property owners overcome market barriers which often discourage investment in energy efficiency and water conservation improvements.

1. Eligible Properties

The Carrollton PACE Program is a strictly voluntary program. All private sector owners of Eligible Properties located within the City’s PACE region may participate in PACE financing. “**Eligible Properties**” include commercial, industrial, and multi-family residential properties with five or more dwelling units. Government, residential¹, and undeveloped property and

¹ This encompasses single family residential and any multi-family properties less than five units.

property undergoing development at the time of the assessment are not included in the definition of Eligible Properties.

2. Qualified Improvements

PACE financing may be used to pay for Qualified Improvements to Eligible Properties. *“Qualified Improvements”* are permanent improvements intended to decrease water or energy consumption or demand, including a product, device, or interacting group of products or devices on the customer’s side of the meter that use energy technology to generate electricity, provide thermal energy, or regulate temperature. Under the PACE Act, products or devices that are not permanently fixed to real property are not considered to be Qualified Improvements.

The following items may constitute Qualified Improvements:

- High efficiency heating, ventilating and air conditioning (“HVAC”) systems
- High efficiency chillers, boilers, and furnaces
- High efficiency water heating systems
- Energy management systems and controls
- Distributed generation systems
- High efficiency lighting system upgrades
- Building enclosure and envelope improvements
- Water conservation and wastewater recovery and reuse systems
- Combustion and burner upgrades
- Heat recovery and steam traps
- Water management systems and controls (indoor and outdoor)
- High efficiency irrigation equipment

3. Benefits of PACE to Property Owners

The PACE program will enable owners of Eligible Properties to overcome traditional barriers to capital investments in energy efficiency and water conservation improvements, such as unattractive returns on investment, split incentives between landlords and tenants, and uncertainty of recouping the investment upon sale of the property.

By financing Qualified Improvements through the program, property owners may achieve utility cost savings that exceed the amount of the assessment and reduce their exposure to utility price volatility. As a result, the value of the property will be enhanced, and the owner will only be obligated to pay the assessment installments that accrue during its period of ownership of the property. Additionally, by investing in energy efficiency and water conservation with PACE financing, property owners may also qualify for various rebate, tax credit, and incentive programs offered by utility providers and state or federal governmental authorities to encourage these types of investments.

4. Benefits of PACE to the City

Among other things, projects financed through the Carrollton PACE Program will:

- Enable property owners and occupants to save substantial amounts in utility costs;
- Reduce demand on the electricity grid;
- Mitigate greenhouse gas emissions associated with energy generation;
- Enhance the value and efficiency of existing buildings;
- Boost the local economy by creating new job opportunities for laborers and new business opportunities for contractors, engineers, commercial lenders, professionals, and equipment vendors and manufactures;
- Increase business retention and expansion in the PACE region by enabling cost effective energy and water saving updates to existing property;
- Improve productivity through optimized energy usage;
- Support the State’s water conservation plan; and
- Better enable the City to meet its water conservation goals.

Finally, EPA regulations have significant impacts on air quality standards in Texas. For example, the recent adjustment in the NAAQS to a lower standard increased the difficulty for the area to maintain its attainment status. Being non-attainment for priority pollutants in the Clean Air Act endangers federal transportation funding. Through the reduction in energy consumption, as a result of the PACE program, there will be a decreased demand for power resulting in lower emissions from power plants.

The PACE program requires minimal support from the City. It is designed to be self-sustaining. Furthermore, because the PACE program is tax neutral, it achieves all of the benefits listed in this Report without imposing a burden on the City’s general fund.

The 84th Texas Legislature added a provision that explicitly provides immunity to the City and its employees, City Council members, and board members, executives, employees, and contractors of a third party who enter into a contract with a local government to provide administrative services for a program under this chapter.²

5. The Benefits of PACE to Lenders

PACE loans are attractive to lenders because they are very secure investments. Like a property tax lien, the assessment lien securing the PACE loan has priority over other liens on the property. Therefore, the risk of loss from non-payment of a PACE loan is low compared to most other types of loans. PACE assessments provide lenders with an attractive new product to assist existing and new customers in addressing an almost universal pent-up demand for needed commercial and industrial property equipment modernization. In order to protect the interests of holders of existing mortgage loans on the property, the PACE Act requires their written consent to the PACE assessment as a condition to obtaining a PACE loan.

² TX. Local Gov’t Code §399.019. In the 85th legislature, HB 2654 clarified that the personal immunity provisions apply to all elected officials performing rights and duties under chapter 399 of the Local Government Code.

6. The Benefits of PACE to Contractors, Engineers, and Manufacturers

PACE loans provide attractive sources of financing for water and energy saving retrofits and upgrades, thereby encouraging property owners to make substantial investments in existing commercial and industrial buildings. As a result, PACE will unlock business opportunities for contractors, engineers, and manufacturers throughout the commercial and industrial sectors.

7. Administration of the PACE Program

Under the PACE Act, the establishment and operation of the program are considered to be governmental functions. The PACE Act further authorizes the City to enter into a contract with a third party to provide administrative services for the PACE program (the “*Authorized Representative*”). The City may delegate administration of the PACE program to a qualified, non-profit organization that can administer the program at no cost to the City.

The Authorized Representative’s role is oversight of the program to ensure best practices and consumer protections at the lowest possible cost to the property owner. The administrator’s role does not include selecting participants (other than setting objective standards to maintain quality control). The Authorized Representative may not offer services that compete with the PACE market the authorized representative is responsible for overseeing.

The Authorized Representative will be funded by administrative fees paid by the property owners establishing a PACE project, charitable grants, or other sources of revenue. The Authorized Representative will not receive compensation or reimbursement from the City. The Authorized Representative may not impose any fees directly or indirectly not authorized in advance by the City in writing. The Authorized Representative is prohibited from charging fees to participate in the program.

Periodic updates to the standard form documents (described in Section 9) will be necessary as the program evolves, incorporating best practices and standardizing the PACE contracts across various PACE programs. **The Authorized Representative will be tasked with maintaining the form contracts and recommending technical and conforming updates, as necessary, for City Council consideration and approval.** ~~The Authorized Representative will be tasked with maintaining the form contracts and making technical and conforming updates as necessary so long as the changes are consistent with the resolution to establish the PACE program and the statute~~

8. Eligible Lenders

The PACE Act does not set criteria for financial institutions or investors to be PACE lenders. The City will follow best practices of other PACE programs by recommending that lenders be:

- Any federally insured depository institution such as a bank, savings bank, savings and loan association and federal or state credit union;
- Any insurance company authorized to conduct business in one or more states;

- Any registered investment company, registered business development company, or a small business
- Small business investment company;
- Any publicly traded entity; or
- Any private entity that:
 - Has a minimum net worth of \$5 million; and
 - Has at least three years' experience in business or industrial lending or commercial real estate lending (including multifamily lending), or has a lending officer that has at least three years' experience in business or industrial lending or commercial real estate lending; and
 - Can provide independent certification as to availability of funds; and
- All lenders must have the ability to carry out, either directly or through a servicer, the bookkeeping and customer service work necessary to manage the assessment accounts.

Any lender can participate in the Carrollton PACE Program as long as it is a financially stable entity with the ability to carry out, either directly or through a servicer, the bookkeeping and customer service work necessary to manage the assessment accounts. The property owner, not the City or the Authorized Representative, selects the lender.

The Authorized Representative will not guarantee or imply that funding will automatically be provided from a third-party lender, imply or create any endorsement of, or responsibility for, any lender, or create any type of express or implied favoritism for any eligible lender.

9. Components of the PACE Program

As required under Section 399.009 of the PACE Act, the following describes all aspects of the PACE Program:

- a. Map of Region. A map of the boundaries of the region included in the program is attached to this Report as Exhibit 1. The region encompasses the City limits.
- b. Form Contract With Owner. A form contract between the City and the record owner of the Eligible Property is attached as Exhibit 2. It specifies the terms of the assessment under the Carrollton PACE Program and the financing to be provided by an Eligible Lender of the property owner's choosing.
- c. Form Contract with Lender. A form contract between the City and the Eligible Lender chosen by a property owner is attached to this Report as Exhibit 3. It specifies the financing and servicing of the debt through assessments.
- d. Form Notice of Contractual Assessment Lien. A form Notice of Assessment Lien to be filed by the **Authorized Representative, on behalf of the City**, with the County Clerk, depending on where the Eligible Property is located, is attached to this Report as Exhibit 4.

e. Qualified Improvement. The following types of projects are qualified improvements that may be subject to contractual assessments under the Carrollton PACE Program:

Projects that: (a) involve the installation or modification of a permanent improvement fixed to privately owned commercial, industrial or residential real property with five (5) or more dwelling units;³ and (b) are intended to decrease energy or water consumption or demand by installing a product, device, or interacting group of products or devices on the customer's side of the meter that uses energy technology to generate electricity, provide thermal energy, or regulate temperature.⁴

A sample list of potential Qualified Improvements appears in Section 2 above.

The Carrollton PACE Program may not be used to finance improvements to undeveloped lots or lots undergoing development at the time of the assessment, or for the purchase or installation of products or devices not permanently fixed to real property.⁵

The Carrollton PACE Program may be used to finance improvements on property being redeveloped for the allowable valuation of the permanent improvement intended to decrease energy or water consumption or demand that exceeds the requirements of the City Code of Ordinances, as amended, as determined by an independent third party in accordance with the Carrollton PACE Program technical specifications.

f. Authorized Representative. HB 3187 was signed into law on June 16, 2015. It authorizes the City to delegate administration of the PACE program to a third-party "representative." The City Council will approve all individual projects, on a case by case basis. Upon approval of a project, the City may delegate all other official administrative responsibilities, like the execution of individual contracts with property owners and lenders, to an Authorized Representative. This relationship will be monitored and maintained by the City Manager or her designee.

g. Plans for Insuring Sufficient Capital⁶. Lenders will extend loans to finance Qualified Improvements. Financing documents executed between owners and lenders will impose a contractual assessment on Eligible Property to repay the owner's financing of the Qualified Improvements. The lenders will ensure that property owners demonstrate

³ TX. Local Gov't Code §399.002(5).

⁴ TX. Local Gov't Code §399.002(3).

⁵ TX. Local Gov't Code §399.004.

⁶ The Texas PACE Authority's website (www.texaspaceauthority.org) offers a non-exhaustive list of interested and qualified lenders to assist property owners in funding PACE projects in Texas.

the financial ability to fulfill the financial obligations to be repaid through contractual assessments.

h. No Use of Bonds or Public Funds. The City does not intend to issue bonds or use any other public monies to fund PACE projects. Property owners will obtain all financing from the Eligible Lenders they choose.

i. Limit on Length of Loan. One of the statutory criteria of a PACE loan is that the assessment payment period cannot exceed the useful life of the Qualified Improvement that is the basis for the loan and assessment. As part of the application process, the property owners will submit a third-party review showing the water or energy baseline conditions and the projected water or energy savings. This review will aid the Authorized Representative in making a determination that the period of the requested assessment does not exceed the useful life of the Qualified Improvement.

j. Application Process. The Authorized Representative will accept applications from property owners seeking to finance Qualified Improvements under the program. Each application must be accompanied by the required application fee and must include:

- (1) A description of the specific Qualified Improvements to be installed or modified on the property;
- (2) A description of the specific real property to which the qualified improvements will be permanently fixed; and
- (3) The total amount of financing, including any transaction costs, to be repaid through assessments.

Based on this information, the Authorized Representative may issue a preliminary letter indicating that, subject to verification of all requirements at closing, the proposed project appears to meet program requirements. Based on this preliminary letter, the property owner may initiate an independent third-party review of the project and submit the project to Eligible Lenders for approval of financing.

Once the above processes are completed, the property owner will submit the application to the Authorized Representative to obtain **project approval from the City Council**. The property owner is expected to produce the following documentation prior to consideration by City Council and closing on the PACE loan:

- (1) A Report conducted by a qualified, independent third party, showing water or energy baseline conditions and the projected water or energy savings, or the amount of renewable energy generated attributable to the project;
- (2) Such financial information about the owner and the property as the lender chosen by the owner deems necessary to determine that the owner has demonstrated the financial ability to fulfill the financial obligations to be paid through assessments; and
- (3) All other information required by the Authorized Representative.

k. Financial Eligibility Requirements. The Authorized Representative will determine whether the owner, the property and the improvements are eligible for financing under the program and provide such information to City Council for project approval. The Eligible Lender chosen by the owner will determine whether the owner has demonstrated the financial ability to repay the financial obligations to be collected through contractual assessments. The statutory method⁷ for ensuring such a demonstration of financial ability must be based on appropriate underwriting factors, including the following:

- (1) verification that the person requesting to participate in the program is the legal record owner of the benefitted property;
- (2) the applicant is current on mortgage and property tax payments;
- (3) the applicant is not insolvent or in bankruptcy proceedings;
- (4) the title of the benefitted property is not in dispute; and
- (5) there is an appropriate ratio of the amount of the assessment to the assessed value of the property.

l. Mortgage Holder Notice and Consent. As a condition to the execution of a written contract between the Authorized Representative and the property owner imposing an assessment under the program, the holder of any mortgage lien on the property must be given notice of the owner's intention to participate in the program on or before the 30th day before the date the contract is executed, and the owner must obtain the written consent of all mortgage holders.⁸

m. Imposition of Assessment. The Authorized Representative will enter into a written contract with the property owner, only after:

- (1) City Council approval of the project;
- (2) The property owner delivers to the Authorized Representative written consent of all mortgage lien holders;
- (3) The Authorized Representative's determination that the owner and the property are eligible to participate in the program, that the proposed improvements are reasonably likely to decrease energy or water consumption or demand, and that the period of the requested assessment does not exceed the useful life of the Qualified Improvements; and
- (4) The Eligible Lender notifies the Authorized Representative that the owner has demonstrated the financial ability to fulfill the financial obligations to be repaid through contractual assessments.

The contract will impose a contractual assessment on the owner's Eligible Property to repay the lender's financing of the Qualified Improvements. The Eligible Lender will file "A Notice of Contractual Assessment Lien," in substantially the form in Exhibit 4 in the Official Public Records of the County, depending on where the Eligible Property is

⁷ TX. Local Gov't Code §399.009(b).

⁸ TX. Local Gov't Code §399.010.

located, as notice to the public of the assessment, from the date of filing. The contract and the notice must contain the amount of the assessment, the legal description of the property, the name of the property owner, and a reference to the statutory assessment lien provided under the PACE Act.

n. Collection of Assessments. The execution of the written contract between the Authorized Representative and the property owner and recording of the Notice of Contractual Assessment Lien incorporate the terms of the financing documents executed between the property owner and with the lender to repay the financing secured by the assessment. The third-party lender will advance financing to the owner, and the terms for repayment will be such terms as are agreed between the lender and the owner. Under the form lender contract attached as Exhibit 3, the lender or a designated servicer will agree to service the debt secured by the assessment.⁹

With funds from the lender, the property owner can purchase directly the equipment and materials for the Qualified Improvement and contract directly, including through lease, power purchase agreement, or other service contract, for the installation or modification of the Qualified Improvements. Alternatively, the lender may make progress payments to the property owner as the Qualified Improvement is installed.

The lender will receive the owner's assessment payments to repay the debt and remit to the Authorized Representative any administrative fees. The lender will have the right to assign or transfer the right to receive the installments of the debt secured by the assessment, provided all of the following conditions are met:

- (1) The assignment or transfer is made to an Eligible Lender, as defined above;
- (2) The property owner and the Authorized Representative are notified in writing of the assignment or transfer and the address to which payment of the future installments should be mailed at least thirty (30) days before the next installment is due according to the schedule for repayment of the debt; and
- (3) The assignee or transferee, by operation of the financing documents or otherwise, written evidence of which shall be provided, assumes lender's obligations under the lender contract.

o. Verification Review. After a Qualified Improvement is completed, the Authorized Representative will require the property owner to provide verification by a qualified independent third-party reviewer that the Qualified Improvement was properly completed and is operating as intended.¹⁰ The verification report conclusively establishes that the improvement is a Qualified Improvement and the project is qualified under the Carrollton PACE Program.

⁹ The servicer will be responsible for maintaining payment records, account balances, and reporting to the Authorized Representative as required.

¹⁰ TX. Local Gov't Code §399.011.

p. Marketing and Education Services. The City may subsequently enter into agreements with one or more other local governments or non-profit organizations that promote energy and water conservation and/or economic development to provide marketing and education services for the Carrollton PACE Program. The Authorized Representative will provide service provider training workshops for contractors, engineers, property managers, and other stakeholders, provide outreach and education for all stakeholders including presentations, conference booths, and individual meetings, and provide written and electronic materials such as case studies, flyers, and webinars.

q. Quality Assurance and Antifraud Measures. The Authorized Representative will institute quality assurance and antifraud measures for the Carrollton PACE Program. The Authorized Representative will review each PACE application for completeness and supporting documents through independent review and verification procedures. The application and required attachments will identify and supply the information necessary to ensure that the property owner, the property itself, and the proposed project all satisfy Carrollton PACE Program underwriting and technical standard requirements. Measures will be put in place to provide safeguards, including a review of the energy and water savings baseline and certification of compliance with the technical standards manual from an independent third-party reviewer (ITPR), who must be a registered professional engineer, before the project can proceed. This review will include a site visit, report, and a letter from the ITPR certifying that he or she has no financial interest in the project and is an independent reviewer. After the construction of the project is complete, an ITPR will conduct a final site inspection and determine whether the project was completed and is operating properly. The reviewer's certification will also include a statement that the reviewer is qualified and has no financial interest in the project.

r. Delinquency. Under the terms of the form lender contract attached as Exhibit 3, if a property owner fails to pay an agreed installment when due on the PACE assessment, the lender will agree to take at least the following steps to collect the delinquent installment:

- (1) Mail to the owner a written notice of delinquency and demand for payment by both certified mail (return receipt requested) and first class mail, and
- (2) Mail to the owner a second notice of delinquency and demand for payment by both certified mail (return receipt requested) and first class mail, at least thirty (30) days after the date of the first notice if the delinquency is continuing.

If the owner fails to cure the delinquency within 30 days after mailing the second notice of delinquency, the lender may notify the Authorized Representative of the owner's default. Pursuant to Texas Local Government Code Section 399.014(c), the Authorized Representative will initiate steps for the City to enforce the assessment lien, **at the lender's sole expense**, in the same manner as a property tax lien against real property may be enforced, to the extent the enforcement is consistent with Section 50, Article XVI, of

the Texas Constitution. Delinquent installments will incur penalties and interest in the same manner and at the same rate as delinquent property taxes, according to Texas Local Government Code Section 399.014(d), and such statutory penalties and interest will be due to the lender to offset the cost of collection.

If the City files suit to enforce collection, the City may also recover costs and expenses, including attorney's fees, in a suit to collect a delinquent installment of an assessment in the same manner and at the same rate as in suit to collect a delinquent property tax. If a delinquent installment of an assessment is collected after the filing of a suit, the City will remit to the lender the net amount of the delinquent installments and contractual interest collected and remit to the Authorized Representative the amount of any administrative fees collected. The City will retain any statutory penalties, interest, and attorney's fees collected necessary to reimburse it to enforce any provision of the Carrollton PACE Program, and any remaining attorney's fees will be remitted to lender to reimburse it for the cost of collection.

10. Limitations.

The Carrollton PACE Program shall not give rise to or create a charge against the general credit or taxing power of the City or a debt or other obligation of the City payable from any source. No City funds, revenues, taxes, or income of any kind shall be used to pay a contractual assessment, filing fee, collection cost, litigation cost, or any other expense arising under the Carrollton PACE Program. The Carrollton PACE Program is created to provide a third-party financing mechanism for energy saving betterments; no alternate financing is approved through the approval of the Carrollton PACE Program. The City assumes no financial obligation whatsoever in the event of default or foreclosure of any kind. None of the City or any of its elected or appointed officials or any of its officers or employees shall incur any liability hereunder to an owner, the Authorized Representative, a lender, or any other party in their individual capacities by reason of the Carrollton PACE Program or their acts or omissions under the Carrollton PACE Program.

Further, any owner, Authorized Representative, or lender taking part in the Carrollton PACE Program shall indemnify and hold harmless the City and any of its elected or appointed officials or any of its officers or employees from any and all claims, causes of actions, or suits arising from or related to the Carrollton PACE Program.