

# **State of Colorado** **Office of the State Auditor**

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## Performance Audit of the Colorado New Energy Improvement District

May 2019



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May 24, 2019

Members of the Legislative Audit Committee:

This report contains the results of a performance audit of the Colorado New Energy Improvement District (District). The audit was conducted pursuant to Section 2-3-120, C.R.S., which requires the State Auditor to conduct a performance audit of the District and its new energy improvement program every five years. The State Auditor contracted with Sjoberg Evashenk Consulting, Inc., to conduct this audit. The report presents our findings, conclusions, and recommendations, and the responses of the District's Board of Directors.

Respectfully submitted,

A handwritten signature in blue ink that reads "George J. Skiles".

George J. Skiles  
Principal

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# REPORT HIGHLIGHTS

## Colorado New Energy Improvement District

Performance Audit, May 2019

### AUDIT CONCERN

Revenues from program administration fees paid by property owners participating in the C-PACE Program have yet to be sufficient to cover the District's operating costs.

### KEY FINDINGS

- The District's goal is to be self-sustaining through program administration fees paid by property owners who participate in the C-PACE Program. However, new project activity and the related program administration fee revenue is not yet at a breakeven level:
  - In 2018, the District collected about \$500,000 in program administration fees, and its operating expenditures were nearly \$630,000. For 2019, the District projected about \$1.125 million in revenues from program administration fees and about \$1.273 million in operating expenses.
  - The District's forecasts suggest that it needs to close roughly 70 projects per year to reach a sustainable level, which neither the District nor its Program Administrator project will occur until 2020 or 2021.
  - Over the near term, the District remains dependent on grant funds received from the Colorado Energy Office (CEO) to make up for any operating shortfalls. As of March 31, 2019, the District reported an unrestricted fund balance of \$198,000.
- The District has not established a formal management structure that defines the roles and responsibilities of District management separate from the Board of Directors (Board). Since the Board was first appointed in 2013, the CEO-designated Board member has been elected to serve as the Board Chair and, in this capacity, has also served as the District's de facto chief executive/administrator.
- The District continues to rely on CEO staff and resources to help fulfill or support its operations. However, this reliance on CEO also blurs the administrative separation between the District and the State that the General Assembly specified in statute. The District is a separate legal entity that is not an agency of state government nor subject to administrative direction by the State.

### BACKGROUND

The Colorado New Energy Improvement District (District) oversees and administers the Commercial Property Assessed Clean Energy Program (C-PACE Program or Program).

The Program allows commercial property owners to obtain financing for eligible energy efficiency or renewable energy improvements through private third-party lenders. The loans are secured and paid for through a special assessment and corresponding lien that the District places on the property.

The District is governed by a seven-member Board of Directors that includes the CEO Director or his or her designee and six other members appointed by the Governor.

Between 2016 and 2018, the District closed a total of 34 projects totaling approximately \$32.5 million through the C-PACE Program.

### RECOMMENDATIONS

- Continue to adjust the program administration fee, as needed, to encourage new projects while generating sufficient annual revenues to support the District's operations.
- Evaluate and pursue alternative revenue sources, as needed, until the program administration fee-based funding model is fully self-sustaining.
- Establish a formal management structure, including clearly defining the scope, authority, and responsibilities of a chief executive/administrator position that is separate from and accountable to the Board.
- Execute a formal agreement with the CEO that outlines the scope of services, responsibilities, and related compensation for activities that are performed, provided, or supported by CEO employees or resources.

The District agreed with these recommendations.

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# Overview

## Chapter 1

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### Colorado New Energy Improvement District

The Colorado New Energy Improvement District (District) is a statewide special statutory district created to establish, develop, finance, implement, and administer a new energy improvement program (Program) that encourages property owners to invest in energy efficiency or renewable energy improvements to their property.

According to statute, the District constitutes a public instrumentality, and the exercise of its statutory powers and duties is deemed and held to be the performance of an essential public function. However, the District is a separate legal entity that is not an agency of the State or of any local government and is not subject to administrative direction by any department, commission, board, or agency of the State or of any local government [Section 32-20-104(1), C.R.S.].

The District is governed by a seven-member board of directors (Board) that includes the Director of the Colorado Energy Office (CEO) or his or her designee and six additional members, appointed by the Governor for four-year terms, who collectively represent or have executive-level experience in commercial or residential real estate development, financial institutions, the utility industry, and the energy efficiency and renewable energy industries.

The District's boundaries are noncontiguous and include the eligible real property of those property owners who voluntarily join the District through participation in the District's new energy improvement program *and* whose property is located within those counties whose county commission has adopted a resolution authorizing the District to operate the new energy improvement program within its jurisdiction. Twenty-three of Colorado's 64 counties (Adams, Arapahoe, Boulder, Broomfield, Clear Creek, Delta, Denver, Eagle, Fremont, Garfield, Gunnison, Jefferson, Lake, Larimer, Montezuma, Montrose, Ouray, Otero, Pitkin, Pueblo, Routt, San Miguel, and Weld) had authorized such participation as of May 1, 2019, and eligible property owners in seven of these 23 counties had participated in the C-PACE Program.

Because the District does not have general taxing authority, it must rely on revenue from other sources to cover its operating costs. In addition to earning revenue from a program administration fee paid by property owners at project closing, the District has received public grant funding of approximately \$1.3 million. Table 1 provides

data on the District’s operating revenues and expenditures for the first three years of its operations.

**Table 1: Colorado New Energy Improvement District  
Operating Revenues and Expenditures, Calendar Years 2016-2018 (unaudited)**

	Calendar Year		
	2016	2017	2018
<b>Operating Revenues</b>	<b>\$738,000</b>	<b>\$667,000</b>	<b>\$512,000</b>
Grants	\$735,000	\$500,000	\$0
Program Administration Fees	\$3,000	\$167,000	\$501,000
Other <sup>1</sup>	\$0	\$0	\$11,000
<b>Operating Expenditures</b>	<b>\$458,000</b>	<b>\$433,000</b>	<b>\$630,000</b>
Program Administrator Payments	\$392,000	\$398,000	\$451,000
Other District Operations <sup>2</sup>	\$66,000	\$35,000	\$179,000
<b>Ending Fund Balance</b>	<b>\$280,000</b>	<b>\$514,000</b>	<b>\$396,000</b>
Unrestricted	\$268,000	\$506,000	\$365,000
Restricted <sup>3</sup>	\$12,000	\$8,000	\$31,000

Source: Auditor’s analysis of financial data provided by the District. Dollar amounts are rounded to the nearest thousand dollars.

Notes:

<sup>1</sup> Reimbursed expenditures, such as recording fees.

<sup>2</sup> Includes expenditures for bank and recording fees, legal counsel, accounting and auditing services, county fees, insurance, sponsorships, and other miscellaneous costs. Operating expenditures also include the cost of the statutorily required performance audit conducted every five years by the Office of the State Auditor that is paid by the District.

<sup>3</sup> Restricted reserves represent the TABOR Emergency Reserve.

In 2019, the District received additional grant revenues, resulting in a net increase of \$100,000 in funding, and set aside more than \$200,000 of its unrestricted fund balance to fund a statutorily required reserve to mitigate potential losses to participating counties [Section 32-20-107(4)(g), C.R.S.]. As of March 31, 2019, the District reported an unrestricted fund balance of approximately \$198,000.

The District does not currently have any employees, but rather uses contractors for the administration of its new energy improvement program and to provide legal, accounting, and other professional services. The District also relies on staff resources and other in-kind support from CEO. This structure is explained in detail in Chapter 2. The District operates on a December 31 fiscal year end.

### **Property Assessed Clean Energy (PACE) Programs**

According to the U.S. Department of Energy, PACE programs exist for both residential properties (commonly referred to as R-PACE) and commercial properties (commonly referred to as C-PACE). There are some key differences

between R-PACE and C-PACE programs, which has resulted in different rates of adoption and implementation across the United States.

Property owners may be hesitant to invest existing capital or take on additional debt to make energy improvements to their property if they do not expect to own the property long enough for the resulting energy savings to cover the large, up-front costs of the improvements. PACE programs are designed to help overcome this key disincentive by allowing a property owner to finance the cost of energy or other eligible improvements on a property and pay the costs back over time (up to 25 years). Repayment of the loan occurs through a voluntary special assessment on the property that is levied through a “land-secured financing district” (e.g., special district or local improvement district) and collected through the local property tax payment process. In addition to making capital available to property owners, PACE programs are seen as serving the public purposes of reducing energy costs and water use, stimulating the economy, improving property valuation, and creating jobs.

House Bill 10-1328 (the New Energy Jobs Creation Act of 2010) created the District and charged it with establishing and overseeing a statewide PACE program for energy efficiency, renewable energy, and water conservation upgrades on eligible residential real property. However, in July 2010, the Federal Housing Finance Agency (FHFA) issued a statement advising Fannie Mae and Freddie Mac to avoid buying mortgages that have PACE assessments because most PACE loans were the senior liens on the property, taking priority over the mortgage obligation itself. This statement from the FHFA effectively stalled the development of the District’s residential PACE program. Beginning in 2016, the District started exploring different models of R-PACE based on using a subordinated lien instead of a priority lien to address concerns from FHFA. As of May 2019, the District had not implemented a residential PACE program.

Meanwhile, Senate Bill 13-212 (the New Energy Jobs Act of 2013) expanded the scope of the District and refocused its statewide PACE program on making improvements to *commercial* properties, which is described in more detail in the following section. Commercial properties were not included in the FHFA’s 2010 opposition statement.

## **The District’s Commercial Property Assessed Clean Energy Program**

The District’s new energy improvement program, known as the Commercial Property Assessed Clean Energy Program (C-PACE Program or Program), allows owners of existing commercial or multifamily buildings (i.e., five or more units) to finance qualifying energy efficiency, renewable energy generation, water conservation, and other energy improvements. The Program also permits the financing of qualifying energy improvements on new commercial construction.

Improvements that are eligible under the Program typically fall into one of two categories, as follows:

- **Energy efficiency improvements** are installations or modifications that are designed to reduce energy and/or water consumption, such as:
  - Insulation in walls, roofs, floors, and foundations and in heating and cooling distribution systems.
  - Storm windows and doors, multi-glazed windows and doors, heat-absorbing or heat-reflective glazed and coated window and door systems, additional glazing, reductions in glass area, and other window and door system modifications that reduce energy consumption.
  - Automatic energy control systems.
  - Heating, ventilating, or air conditioning and distribution system modifications or replacements in a building.
  - Caulking and weather-stripping and other air sealing measures.
  - Replacement or modification of lighting fixtures and controls to increase the energy efficiency of the system.
  - Energy recovery systems.
  - Daylighting systems (e.g., skylights, controls, light shelves).
  - Combined heat and power (CHP) and waste-to-power projects.
  - Electric vehicle charging equipment added to the building or its associated parking area.
  - Other modification, installation, or remodeling approved as a utility cost-savings measure by the District, including water conservation fixtures, both indoor and outdoor and for both hot and cold water.
- **Renewable energy improvements** are installations or modifications that produce energy from renewable resources, such as photovoltaic, solar thermal, small wind, low-impact hydroelectric, biomass, fuel cell, or geothermal systems (including geothermal heat pumps).

Eligible improvements must be permanently affixed or not easily removable from the property without the use of specialized machinery or tools and without damage to the structure. For this reason, measures that are not permanent (such as the

installation of appliances) are generally not eligible for C-PACE financing unless they are part of a larger package of eligible measures and do not exceed more than 30 percent of the project cost. Authorized improvements financed through the Program may not be removed from the property until the C-PACE assessment lien has been fully repaid.

Eligible improvements may be financed under the Program provided that they generate “utility cost savings,” but there is no statutory requirement that the projects generate positive cash flows based on energy savings. The District encourages property owners to submit projects that have a positive cash flow (i.e., a Savings-to-Investment Ratio (SIR) greater than 1.0) for the following reasons:

- The capital providers (e.g., banks, credit unions, specialty financiers, institutional investors, insurance companies, or other lenders) that provide financing for the projects often look favorably on projects that show positive cash flow over their lifetimes.
- Mortgage holders are more likely to consent to the imposition of the senior C-PACE assessment lien for projects that show positive cash flow.
- In general, the higher the SIR, the greater the demonstrated environmental benefits of the project, helping to promote the statutory goals for the Program.

Table 2 provides general statistics on the C-PACE Program for the first three years of its operations.

**Table 2: Colorado New Energy Improvement District  
C-PACE Program Data, Calendar Years 2016-2018 (unaudited)**

	Calendar Year			Total
	2016	2017	2018	
<b>Number of Projects</b>	3	7	24	<b>34</b>
<b>Total Amount Financed (Dealflow)</b>	\$3,290,000	\$4,493,000	\$24,690,000	<b>\$32,473,000</b>
<b>Lien Assessments<sup>1</sup></b>	n/a	\$44,000	\$615,000	<b>\$659,000</b>
<b>Program Administration Fees</b>	\$3,000	\$167,000	\$501,000	<b>\$671,000</b>
<b>Projected Lifetime Cost Savings</b>	\$2,197,000	\$5,016,000	\$20,985,000	<b>\$28,198,000</b>
<b>Projected Energy Savings (kBTU/yr)<sup>2</sup></b>	3,097,500	14,212,412	35,512,593	<b>50,832,775</b>
<b>Equivalent Number of Cars<sup>3</sup></b>	51.5	236.1	590.0	<b>844.5</b>
<b>Estimated Number of Jobs Created</b>	39.0	54.3	237.3	<b>317.0</b>
<b>Lifetime Emissions Reduction (tons)<sup>4</sup></b>	8,013.4	38,800.0	158,003.0	<b>197,364.4</b>

Source: Auditor’s analysis of C-PACE Program Impact Reports and other data provided by the District. Dollar amounts are rounded to the nearest thousand dollars.

Notes:

<sup>1</sup> Assessments collected by counties through liens placed on property tax rolls, remitted to the District, and passed through to capital providers.

<sup>2</sup> A British Thermal Unit (BTU) measures heat energy and equals the amount of heat needed to raise one pound of water one degree Fahrenheit. A kBTU equals 1,000 BTUs.

<sup>3</sup> The District converts kBTU/yr to a unit of measure more familiar to a layperson. This measure reflects the projected energy savings equal to removing a specific number of vehicles from Colorado roads in a given year.

<sup>4</sup> Carbon dioxide-equivalent emission reductions over the lifetime of the equipment.

### **C-PACE Financing**

C-PACE financing is available for terms of up to 25 years. There is no maximum financing amount available through the Program for improvements to existing properties. However, the financing amount available for improvements to newly constructed properties cannot exceed 20 percent of the total eligible construction cost.

Statute authorizes the District to issue up to \$800 million in special assessment bonds for financing eligible new energy improvement projects and to pay other costs of the District [Section 32-20-108(1), C.R.S.]. However, Senate Bill 13-212 authorized the District to develop a process for funding projects through private third-party financing, rather than through the issuance of bonds. The District has not issued any special assessment bonds to date.

The business model for the District’s C-PACE Program relies fully on private third-party financing for projects. Under this private third-party financing model, the property owner, not the District or the Program, selects the qualified capital provider to provide financing for their approved project. Because C-PACE assessments liens have priority over other liens on the property (described in the

next section), many capital providers view financing for C-PACE projects as less risky than commercial loans, thereby generating attractive interest rates and longer terms for property owners. Property owners are allowed to bring their own capital provider to the project on the condition that the capital provider is qualified to participate in the Program prior to the District's hearing on the assessment lien. The Program also maintains a list of qualified capital providers and, at the property owner's request, will facilitate obtaining basic information about financing terms and conditions from these qualified capital providers for the approved project. The Program does not consider qualified capital providers to be "preferred" providers; all qualified and approved capital providers are eligible to provide C-PACE financing.

### **C-PACE Assessment Lien**

The private third-party financing for eligible projects is secured by a special assessment and corresponding lien that the District places on the subject property. Section 32-20-105(3)(i), C.R.S., requires that property owners receive the consent of all holders of mortgages or deeds of trust on the property prior to the District's imposition of the C-PACE assessment lien. Once the required lienholder consent is obtained, the C-PACE assessment lien on the property is senior to all private liens (mortgages and deeds of trust), is equal in priority to other special assessments on the property, and is junior to general tax liens.

Each county that has authorized the Program to operate within its jurisdiction has agreed to collect the C-PACE assessment from participating property owners via the local property tax collection system, similar to other special assessments, and to remit those funds to the District for distribution to each project's capital provider. Section 30-1-102(1)(c), C.R.S., authorizes county treasurers to collect a service fee equal to 1 percent of the amount of each special assessment payment to support these activities.

A property owner's nonpayment of the C-PACE assessment results in the same consequences as a failure to pay property taxes, including the imposition of penalty interest and fees and, ultimately, a tax lien sale to recover the amounts owed. The District does not have the authority to file a civil action of foreclosure on the subject property.

The C-PACE assessment lien is a debt of property and not the individual property owner(s). Thus, the repayment obligation runs with the property and transfers to the new owner if the property is sold prior to the end of the agreed-upon special assessment period. In connection with any sale, participants agree to make all legally required disclosures about the existence of the C-PACE assessment lien on the property. Ownership of any C-PACE financed improvements on the property transfer to the new owner at the close of the real estate sale.

## **Program Administration**

The District has contracted with a professional services firm to serve as the Program Administrator with responsibility for the day-to-day coordination and delivery of the Program in accordance with the Program Guide adopted by the Board. The Program Administrator's current contract runs through June 30, 2019, with options to extend the term of the agreement through December 31, 2019, and for three additional one-year terms. Payments to the Program Administrator are the District's single largest operating expense item.

The scope of the Program Administrator's responsibilities are significant and fall into three primary areas:

- **Program Management**, which includes responsibilities to:
  - Create, maintain, and update the Program website, including downloadable versions of all Program materials; maintain lists of eligible improvements, qualified capital providers, registered contractors, and participating counties; and conduct case studies of successful projects.
  - Manage project application intake and processing, including ensuring eligibility requirements are met; conduct onsite inspections to verify project installation; and prepare post-construction commissioning oversight reports. These reports provide verification and assurance that the proposed energy efficiency upgrades were installed in accordance with the project requirements and contract documents.
  - Manage a contractor prequalification process that includes application intake and processing and obtaining proof that the contractor has all applicable Colorado state professional licensing.
  - Maintain regular communication with the District, including participating in Board meetings and reporting on Program metrics.
- **Marketing Management**, which includes responsibilities to:
  - Create, maintain, and update all Program materials, including fact sheets, outreach materials, case studies, and frequently asked questions.
  - Manage education and outreach campaigns for property owners, capital providers, contractors, utilities, and counties.

- Provide training sessions for property owners, capital providers, contractors, and counties.
- Maintain regular communication with the District, including participating in Board meetings and reporting on Program metrics.
- **Financial Management**, which includes responsibilities to:
  - Manage capital provider application intake and processing, including ensuring that eligibility requirements are met.
  - Support capital providers during the financial transaction closing process, including coordinating the execution and delivery of all capital provider-focused documentation associated with C-PACE transactions and providing written and verbal guidance as needed for potential contingencies.
  - Coordinate county activities, including District-county contractual agreements for Program participation and assisting county assessors and treasurers with setting up special assessments.
  - Assist the District with annual certification and transmission of certified assessment rolls to county treasurers, processing at the end of the lien, and coordinating the exercise of remedies on default.
  - Maintain regular communication with the District, including participating in Board meetings and reporting on Program metrics.

## **Audit Scope and Methodology**

The Colorado Office of the State Auditor (State Auditor) contracted with Sjoberg Evashenk Consulting, Inc., to conduct this performance audit pursuant to Section 2-3-120, C.R.S., which requires the State Auditor to conduct a performance audit of the District and its new energy improvement program every five years. Audit work was performed from October 2018 through May 2019. We appreciate the cooperation provided by the District and its contractors during the course of this audit.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on the audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The objectives of this audit were to obtain and report background information and data about the District and the C-PACE Program; determine whether the District has sufficient controls in place to ensure effective oversight, monitoring, and reporting related to its activities and the administration of the C-PACE Program; and assess the District's efforts to ensure the future financial sustainability of the District and the C-PACE Program.

To accomplish the audit objectives, we performed the following audit work:

- Reviewed statutes, District bylaws, policies and procedures, Board meeting agendas and minutes, financial records, grant agreements, contracts, and procurement records.
- Interviewed the current and former Board Chairs, the District's Recording Secretary, the District's legal counsel, and the C-PACE Program Administrator.
- Evaluated performance metrics and workload indicators for the C-PACE Program, including reviewing records for a nonstatistical sample of seven C-PACE projects. The results of our sampling were not projected to the population of all C-PACE projects.
- Performed limited research on statewide C-PACE programs operating in eight other states.

We planned our audit work to assess the development of the District since the General Assembly created it in 2010, its progress toward achieving a sustainable business model, and those internal controls that were significant to the audit objectives. Our conclusions on the effectiveness of those controls, as well as specific details about the audit work supporting our findings, conclusions, and recommendations, are described in the remainder of this report.

A draft of this report was reviewed by the District. We have incorporated the District's comments into the report where relevant and appropriate. The written responses to the recommendations and the related implementation dates are the sole responsibility of the District.

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# District Sustainability

## Chapter 2

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The General Assembly created the Colorado New Energy Improvement District (District) in 2010 as a special statutory district to establish, develop, finance, and administer a new energy improvement program [Section 32-20-105, C.R.S.].

In order to allow the District to achieve its purpose, statute grants the District a number of general powers and duties, including the following:

- To have perpetual existence.
- To adopt bylaws for the regulation of its affairs and conduct of its business.
- To set an annual budget.
- To enter into contracts and agreements needed for its functions or operations.
- To acquire, dispose of, and encumber real and personal property needed for its functions or operations.
- To borrow money for the purpose of defraying district expenses, including the funding of appropriate loss reserves.
- To invest any moneys of the District.
- To hire and set the compensation of a Program Administrator and to appoint, hire, retain, and set the compensation of other agents and employees, and to contract for professional services.
- To accept gifts and donations and apply for and accept grants.

The District's Board of Directors (Board) was first appointed by the Governor in 2013, and the District contracted with its Program Administrator for the C-PACE Program in December 2015. Between 2015 and 2017, most of the District's structure and operations were developed and refined, including establishing Program guidelines and protocols; starting Program services and operations; marketing the Program to commercial property owners, construction firms, counties, capital providers, and other key stakeholders; establishing the District's legal and accounting services and related administrative processes; and finalizing

essential Program documents. The District successfully closed on its first funded project in 2016.

The District and its C-PACE Program are still relatively young in their organizational development. Overall, we found that the District has taken reasonable steps and exhibited due diligence during its start-up and early growth years to implement administrative operations, processes, and key controls to ensure (1) compliance with statutory requirements and Program guidelines, (2) the proper accounting and use of District revenues and expenditures, and (3) adequate oversight and governance of Program and District activities and the professional services firms that support them. However, in the remainder of this chapter we discuss ongoing challenges with the District's program administration fee-based revenue model and the need to formalize the District's management structure. Both of these areas are critical for the continued growth and long-term sustainability of the District and the C-PACE Program.

## Financial Sustainability

The District does not have general taxing authority. When creating the District, the General Assembly also did not provide any state appropriations. Thus, the revenues needed to support the District must come from other sources. Statute provides three mechanisms through which the District is authorized to generate operating revenues:

- **Fees.** Pursuant to Section 32-20-105(3), C.R.S., which authorizes the District to charge program fees, the District established a one-time “program administration fee” charged to participating property owners based on a percentage of the total financed project amount. The District relies on the program administration fee to help fund the District's operating costs, including payments to its Program Administrator for the day-to-day administration of the C-PACE Program.

Between 2016 and 2018, the program administration fee was set at 2.5 percent of the total eligible financed project amount not to exceed \$75,000 per project. In 2016 and 2017, the full amount of this fee was paid to the Program Administrator as compensation for administering the Program. Starting in January 2018, the District began retaining 10 percent of the fee (0.25 percent of the total financed project amount) with the remaining 90 percent of the fee (2.25 percent of the total financed project amount) going to the Program Administrator. Beginning in March 2018, the District kept the program administration fee set at 2.5 percent of the total financed project amount, but lowered the maximum to \$50,000 per project. In January 2019, the District increased its share of the program administration

fee to 15 percent (0.375 percent of the total financed project amount) with the remaining 85 percent (2.125 percent of the total financed project amount) going to the Program Administrator.

- **Grants.** Section 32-20-105(2)(1), C.R.S., authorizes the District to apply for and accept grants. To date, the District has relied on three grants totaling \$1.335 million from the Colorado Energy Office (CEO) to provide seed funding for the start-up of the C-PACE Program and District operations. In February 2016, the District was awarded a \$735,000 grant, which it used to launch the Program, fund administrative services, and begin to build its general administrative infrastructure. In March 2017, the District was awarded a second grant totaling \$500,000 to fund a reserve to mitigate county concerns related to the possible impacts of potential defaults. In January 2019, the District returned \$200,000 from the second grant to CEO because the county reserve fund requirements were met, and was awarded a third grant totaling \$300,000 to help pay the District's operating costs.
- **Bond Proceeds.** Section 32-20-108(1), C.R.S., authorizes the District to issue special assessment bonds in an aggregate principal amount up to \$800 million for the purpose of generating the moneys needed to make reimbursement or direct payment to District members for eligible projects and to pay other costs of the District. If issued, the bonds would be secured by the District's ability to place special assessment liens on subject properties. Because the District's business model currently relies on private third-party capital providers to finance all C-PACE projects, the District has not issued any special assessment bonds to date. However, the District's bonding authority remains authorized in statute.

### **What audit work was performed and what was the purpose?**

We interviewed District representatives and reviewed data and documentation pertaining to the District's operating budgets, revenues, and expenditures; the program administration fee structure; and reports, analyses, forecasts, and projections prepared by the District and the Program Administrator based on current fee levels and projected Program activity.

The purpose of the audit work was to assess the District's efforts to ensure its long-term financial sustainability through the program administration fee-based revenue model adopted by the Board. We did not focus on the role that grant revenues or bond proceeds could potentially play in the District's long-term financial outlook.

## **How were the results of the audit work measured?**

Although the District has relied on grant funds to support operating activities during its formative years, the District's long-term goal is for the District and the C-PACE Program be self-sustaining through revenues from program administration fees charged to participating property owners. Therefore, determining and setting the fee at a level that will be self-sustaining requires the District to balance several factors, including:

- The amount that property owners are willing to pay in administration fees to access the C-PACE financing mechanism for their projects.
- The annual revenue needed to cover the District's ongoing operating costs, including its contract payments to the Program Administrator.
- The level of compensation needed to attract and retain the Program Administrator.

## **What problem did the audit work identify and why did it occur?**

Our review of the District's financial information, as well as projections prepared by the District of project volume (i.e., the number of projects completed), dealflow (i.e., the aggregate dollar value of the projects), and the resulting program administration fees, show that the District's program administration fee structure has not yet produced sufficient revenues to cover the District's operating costs.

The District has developed a range of projections from optimistic to conservative for its existing fee structure, as well as for variations of its fee structure, such as higher or lower caps on the program administration fee or modified splits between the District's and Program Administrator's respective portions of the fee. The District's projections are point-in-time estimates based on a number of different variables and assumptions. The data in Table 3 show an average 3-year projection developed by the District that is neither overly conservative nor overly optimistic. We provide this detail to help illustrate that, based on project administration fee revenue alone, the District is at risk of negative or only slightly positive operating cash flows through 2021, even when, for example, the number of new projects in 2021 is projected to be roughly triple the number of new projects the District had in 2018. Neither the District nor the Program Administrator forecast new project activity to reach a breakeven level for the District until 2020 or 2021.

**Table 3: Colorado New Energy Improvement District  
Estimated Operating Revenues, Expenses, and Cash Flow  
Calendar Years 2019-2021 (unaudited)  
(as of January 2019)**

	<b>Projected</b>		
	<b>2019</b>	<b>2020</b>	<b>2021</b>
<b>Number of New Projects</b>	47	68	74
<b>Dealflow</b>	\$49,500,000	\$71,750,000	\$81,250,000
<b>Program Administration Fees</b>	\$1,125,000	\$1,644,000	\$1,856,000
<b>Estimated Operating Revenues</b>	<b>\$1,125,000</b>	<b>\$1,644,000</b>	<b>\$1,856,000</b>
Program Administration Fee (85% Share for Program Administrator)	\$956,000	\$1,397,000	\$1,578,000
Program Administration Fee (15% Share for District)	\$169,000	\$247,000	\$278,000
<b>Estimated Operating Expenses</b>	<b>\$1,273,000</b>	<b>\$1,617,000</b>	<b>\$1,798,000</b>
Program Administrator Payments	\$956,000	\$1,397,000	\$1,578,000
All Other Operating Expenses <sup>1</sup>	\$317,000	\$220,000	\$220,000
<b>Estimated Operating Cash Flow</b>	<b>(\$148,000)</b>	<b>\$27,000</b>	<b>\$58,000</b>
Source: Auditor's analysis of financial and program data provided by the District. Dollar amounts are rounded to the nearest thousand dollars.			
Notes:			
<sup>1</sup> Estimated operating expenses for 2019 are higher due to the cost of the statutorily required performance audit conducted every five years by the Office of the State Auditor that is paid by the District.			

Because new project activity and the related program administration fee revenue is not yet at a breakeven level, the District's financial sustainability over the near term remains dependent on grant funds received from CEO to make up for any operating shortfalls. As described previously, as of March 31, 2019, the District reported an unrestricted fund balance of approximately \$198,000. Although the District has pursued additional grant funds to address projected cash flow shortages, relying on grant funds for general operating support still poses a sustainability risk for the organization should future grant funds no longer be available. Granting agencies also may attach restrictions or parameters on how funds can be used.

Over the long term, the District's ability to become and remain self-sustaining through a program administration fee-based funding model is based on its ability to successfully balance a number of interrelated factors, as discussed in the following sections.

## Project Volume

Fundamentally, the District’s ability to generate sufficient revenue from the program administration fee to sustain its operations is predicated on its ability to build project leads and attain sufficient participation in the Program (i.e., new projects), including a sufficient number of high-dollar projects. Project volume is determined by the overall market for the Program, which is driven by factors such as the number of commercial properties within counties that have authorized participation in the Program, the desire of property owners to invest in energy improvements, and the property owners’ need and willingness to incur the program administration fee to pursue C-PACE financing for these projects. As of May 1 2019, there were 23 counties participating in the Program encompassing approximately 71 percent of Colorado’s commercial building stock.

Over the past three years, projects financed through the Program have ranged from approximately \$53,900 to more than \$4.25 million per project. Table 4 shows the collection and allocation of the program administration fee revenue for the first three years of the C-PACE Program’s operations. Even with the Program becoming more robust and the number of projects closed increasing by eight times, the District earned less than \$50,000 in total fee revenue during this period to cover operating costs other than its payments to the Program Administrator.

**Table 4: Colorado New Energy Improvement District  
C-PACE Projects and Program Administration Fee Collections  
Calendar Years 2016-2018 (unaudited)**

	Calendar Year			Total
	2016	2017	2018	
<b>Projects Closed</b>	3	7	24	<b>34</b>
<b>Dealflow</b>	\$3.3 million	\$4.5 million	\$24.7 million	<b>\$32.5 million</b>
<b>Program Administration Fees Collected<sup>1</sup></b>	\$3,000	\$167,000	\$501,000	<b>\$671,000</b>
District Share	N/A	N/A	\$50,000	<b>\$50,000</b>
Program Administrator Share	\$3,000	\$167,000	\$451,000	<b>\$621,000</b>

Source: Auditor’s analysis of financial and program data provided by the District. Dollar amounts are rounded to the nearest thousand dollars.

Notes:

<sup>1</sup> Prior to 2018, the District did not retain a percentage of the program administration fee; the full amount was paid to the Program Administrator. In January 2018, the District began retaining 10 percent of the program administration fee, which was assessed at 2.5 percent of the total financed project amount not to exceed \$75,000, and, in March 2018, lowered this not-to-exceed amount to \$50,000. Starting in 2019, the District increased its share to 15 percent of the program administration fee, which is assessed at 2.5 percent of the total financed project amount not to exceed \$50,000.

According to District projections, in order to achieve a dealflow that results in fee revenues sufficient to cover its operating costs, the District will need to close approximately 70 new projects of varying magnitudes each year (e.g., 44 projects under \$1 million and 26 projects over \$1 million). As a start-up organization, the observed trends of increasing numbers of projects and the resulting dealflow are moving in the right direction. However, the District has not yet achieved the volume of projects required to make its program administration fee-based model sustainable.

The District has continued to adjust its administration fee structure as the District's operations have evolved. For example, the District's reduction in the cap on the program administration fee, which took effect in March 2018, was intended to stimulate market demand by making it less costly for property owners to participate in the Program. However, this reduction also reduced the District's maximum per-project revenue potential from \$7,500 to \$5,000, thereby placing additional pressure on the District to achieve substantial increases in the number of new projects.

### **Fee Structure**

Overall, the District is relying on a funding model for the C-PACE Program whereby the cost of the District's support services for *existing* assessment liens are entirely dependent upon and funded through program administration fee revenues generated by *new* projects. However, the District is legally responsible for providing assessment support services over the life of the existing C-PACE assessment liens, which can be up to 25 years [Section 32-20-106(4), C.R.S.].

The District's C-PACE operations can be broken down into two core activities—project-specific administration and assessment support services:

- Project-specific administration activities occur when a new project is financed and recorded and include activities such as preparation of assessing resolutions, conducting the Board's assessment hearing, obtaining and documenting lender consent from each party holding a pre-existing lien on the subject property, and recording the lien package following closing.
- Assessment support services occur on an annual basis and include activities such as providing certified assessment rolls to each county by the December 1 annual statutory deadline, collecting assessment payments from counties, and remitting the payments to the capital providers.

Table 5 shows how, over a relatively short period of time, the District’s workload for servicing existing C-PACE assessment liens will grow in volume as the number of new project closings increases.

**Table 5: Actual and Projected Volume of C-PACE Assessment Liens  
Calendar Years 2016-2021**

	Calendar Year					
	2016 (Actual)	2017 (Actual)	2018 (Actual)	2019 (Projected)	2020 (Projected)	2021 (Projected)
<b>New Assessments</b>	3	7	24	47	68	74
<b>Existing Assessments</b>	3	10	34	81	149	223
Source: Auditor’s analysis of performance reports and internal revenue projections provided by the District.						

It is not unreasonable to foresee a circumstance in which new project activity slows as the result of economic conditions, diminished market demand, or reductions in potential project inventory, leaving the District’s share of program administration fee revenues from new projects insufficient to cover all aspects of the District’s ongoing support services for existing C-PACE assessment liens.

Although the District has the authority to charge program fees, the District has not adopted any mechanism, such as a lien servicing fee, that generates revenues tied directly to its ongoing servicing of *existing* C-PACE assessment liens.

**Program Administrator Costs**

The District has fully outsourced the responsibility for the day-to-day coordination and delivery of the Program. Therefore, the Program Administrator’s ongoing participation is essential to the Program’s long-term sustainability. Financially, the Program Administrator’s compensation is the District’s single largest operating expense item. For example, the District’s payments to the Program Administrator comprised approximately 74 percent of its total operating costs in 2018. The Program Administrator’s compensation, which is also derived from the program administration fee, is another significant factor that the District must consider and balance when setting the fee.

Based upon our review of invoices, it appears that the Program Administrator invested more resources than it was compensated for in the first two years of its contract. Between October 2015 and December 2017, the Program Administrator provided more than \$1.1 million in services on behalf of the District, even though the District paid the Program Administrator about \$630,000 in accordance with the contract. Prior to 2018, the District allocated 100 percent of the program administration fee revenues to the Program Administrator’s compensation. The District’s grant funding from CEO provided the initial funds for the Program Administrator, and the District anticipated that once projects began to close, the

administration fee would produce sufficient revenues to supplant the original grant funding.

It is reasonable that the Program Administrator would be initially willing to spend more than it was paid with the expectation that it will build a robust program that would generate future growth and related revenues. However, the District's changes to the program administration fee cap and the percentage split between the Program Administrator and the District have reduced the maximum amount the Program Administrator can receive as compensation on any given project from \$75,000 to \$42,500, or by 43 percent, which could be a disincentive for the Program Administrator to continue contracting with the District. After the latest fee reduction for 2019, the Program Administrator had only agreed to a six-month contract extension through June 2019. After this time, the District could be without a Program Administrator for the C-PACE Program.

### **Why does this problem matter?**

The General Assembly's intent when creating the District was to make PACE financing available to Coloradans and encourage property owners to make new energy improvements to their properties. Because the business model the Board has chosen for the C-PACE Program relies on private financing, risks to the District's long-term financial sustainability are generally limited to its ability to generate sufficient revenue to cover relatively modest operating costs and to compensate its Program Administrator. Yet, without a viable funding model, the long-term financial sustainability of the District and the C-PACE Program are at risk:

- If the program administration fee is set too high, the District risks driving property owners away from C-PACE financing to other more traditional funding sources or, perhaps, a decision to not pursue their energy improvement project at all.
- If the program administration fee does not generate revenue sufficient to cover the District's operating costs, it will no longer be able to sustain its activities, including paying for outsourced legal and accounting service providers, which provide substantial operational support to the District. The District also will not have the resources necessary to fulfill its long-term obligations for servicing existing C-PACE assessment liens.
- If the District cannot support its operations, specifically servicing existing C-PACE assessment liens, there is a risk that capital providers will not see the revenue stream as reliable, thereby affecting their willingness to provide financing to property owners for future projects. This, in turn, may affect the volume of new projects successfully closed.

- If the program administration fee is not sufficient to support compensation for the Program Administrator that is competitive, the contractor may choose not to continue providing Program administration services to the District. The District does not have the capacity to administer the Program without a Program Administrator. While other firms could provide similar services, it is unclear whether the Program would be financially attractive to another firm if not to the current Program Administrator. At a minimum, loss of the current Program Administrator could temporarily disrupt and effectively stall any new projects under the C-PACE Program.

The District's operating costs will likely increase as its programs grow and mature and its workload increases in scale, scope, and complexity. Thus, unresolved financial sustainability issues could also be a significant barrier to the District's expansion into new program arenas, such as making PACE financing options available to residential property owners.

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### **Recommendation No. 1:**

The Board of Directors for the Colorado New Energy Improvement District (District) should ensure the long-term financial sustainability of the District and the Commercial Property Assessed Clean Energy Program (C-PACE Program or Program) by continuing to:

- a. Adjust the program administration fee, as needed, to encourage new projects while generating sufficient annual revenues to support the District's operations, including the servicing of existing assessment liens and payments to the Program Administrator.
- b. Evaluate and pursue alternative revenue sources, as needed, until the program administration fee-based funding model is fully self-sustaining.

### **District Response:**

- a. Agree. Implementation Date: December 2019 and Ongoing.

The Board agrees that successfully fulfilling our vision for long-term self-sustainable revenues is of paramount importance. In lieu of one-time or annual appropriations from the General Assembly, the Board of Directors ("Board") designed the program to become self-sustaining based on program administration fees collected at project closings. In the initial years of C-PACE Program design and implementation, the District has relied on grant funding to cover operations and create a

project pipeline. The Board is committed to continuing to analyze all revenue sources available to the District, including the District's share of the program administration fee, in order to ensure that the District's operations are adequately supported in future years. Beginning in calendar year 2018, program maturity and project volume growth allowed the District to begin collecting a percentage of the program administration fee collected at each closing. In 2019, the District increased its share of the program administration fee while keeping the overall fee capped at a reasonable level. The Board anticipates adjusting the District's share of the program administration fee as necessary to support the District's core C-PACE Program functions, including project-specific administration activities and assessment support services. Each year, the Board will analyze the sufficiency of projected fee revenue and current cash fund balances to cover administrative costs.

b. Agree. Implementation Date: December 2019 and Ongoing.

The Board agrees and will continue to evaluate and pursue alternative revenue sources, including additional grant funds in 2019 or future years, until the administration fee-based funding model is self-sustaining. While not currently necessary, the Board will take under consideration how a new collections fee could offset the District's annual administrative costs associated with: (1) tracking annual assessment payments received from the counties participating in the C-PACE Program, and (2) remitting said payments back to the qualified capital providers that provided third-party financing to District members. If implemented, the collections fee will need to be designed to not become an impediment to program growth. However, given the expected growth in the C-PACE Program, the District's share of the program administration fee is currently projected to be able to adequately fund the District's core operations. The Board has taken proactive steps to move toward financial self-sustainability and that work will continue each year.

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## District Management

Between 2013, when the Board was first appointed, and 2016, when the District processed its first C-PACE application, the District was primarily focused on working with its contracted Program Administrator to develop and implement the

C-PACE Program. Between 2016 and 2018, the District shifted its focus to increasing the number of projects initiated through the Program. During this time frame, the District also began to establish and expand its administrative operations and was engaged in assessing the viability of launching a residential PACE program in Colorado.

### **What audit work was performed and what was the purpose?**

We reviewed documentation related to the District’s key business processes and internal controls, including draft and final policies and procedures, grant agreements and grant activities, contracts and procurement records, accounts payable and receivable activities, budget processes and adopted budgets, District governance, and monitoring of C-PACE Program activities. We also selected a nonstatistical sample of seven of the 34 C-PACE projects funded as of December 2018 to evaluate compliance with statutory requirements and established Program procedures. Finally, we also interviewed the current and former Board Chairs, the District’s legal counsel, the District’s Recording Secretary, and the C-PACE Program Administrator.

The purpose of the audit work was to evaluate the District’s progress in implementing a system of internal controls necessary to ensure the effective management and oversight of the District’s activities and the C-PACE Program.

### **How were the results of the audit work measured?**

Based on best practices promulgated by the United States Government Accountability Office (GAO) and by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), a “system of internal control” broadly refers to the policies, procedures, processes, systems, and methods that an organization relies on to ensure that it achieves its mission, goals, and objectives on an ongoing basis.

A key characteristic of an effective system of internal control is the separation between management and governance responsibilities:

- **Management.** Management is directly responsible for all activities of an organization, including making decisions regarding the acquisition, deployment, and control of human, financial, physical, and intangible resources. Management is also responsible for the design, implementation, and operating effectiveness of the organization’s system of internal control. For example, management assigns operational responsibilities, establishes written policies and procedures, and monitors personnel and contractors to ensure that programs and activities are being carried out as intended based on direction from the organization’s governing body.

- **Governance.** An organization’s governing body (e.g., board of directors) is responsible for overseeing the strategic direction of the organization and obligations related to the accountability of the organization. This includes overseeing management’s design, implementation, and operation of an internal control system. For some organizations, one or a few members of senior management may also be part of the organization’s governing body. However, the governance role is distinct from that of management.

Additionally, according to organizational life cycle theory, during the start-up phase of an organization, it is not uncommon for a governing board to be involved in performing management functions. However, for organizations in the growth phase and mature organizations, the governing board is generally more of a policy-setting and oversight body that is separate from the management function.

Finally, statute states that “...the [D]istrict shall not be an agency of state government...” and “...shall not be subject to administrative direction by any department, commission, board, or agency of the state.” [Section 32-20-104(1)(a) and (b), C.R.S.].

### **What problem did the audit work identify, why did it occur, and why does it matter?**

We found that the District has taken reasonable steps in the early design, implementation, and operation of its system of internal control to position itself to achieve its objectives and those of the C-PACE Program. However, the District has not taken steps to define and formalize its management structure, including separating management from governance and designating a chief executive/administrator. There is also a lack of clarity and transparency to the relationship between the District and CEO, which effectively blurs the administrative separation between the District and the State that the General Assembly specified in statute.

Ultimately, resolving these fundamental issues with the District’s management structure and its relationship with CEO is critical for the District’s ability to develop into a mature and sustainable organization and deliver on the General Assembly’s policy goals and programmatic outcomes for which the District was created.

### **De Facto Management**

In accordance with Section 32-30-104(2)(a)(I), C.R.S., the CEO Director or his or her designee is a member of the District’s Board of Directors. Since the Board was first appointed in 2013, the CEO-designated Board member has been elected to serve as the Board Chair and, in this capacity, has also served as the District’s de facto chief executive/administrator.

Currently, the District does not employ any part- or full-time personnel, although statute gives the District authority to hire employees or contract for professional services [Section 32-20-105(2)(j)(I), C.R.S.]. Instead, the Board relies entirely on the Board Chair, the Board's Recording Secretary (who is also an employee of CEO), the Program Administrator, and other third-party contractors to carry out the District's operations:

- In 2015, the District contracted with a Program Administrator to administer the C-PACE Program.
- Since 2013, the Board Chair and the District's Recording Secretary performed activities such as developing the District's budget, certifying assessment rolls, completing project close-out procedures, preparing lien packages, processing and accounting for program administration fees, managing and reconciling the District's bank account, processing District invoices, performing accounting and procurement functions, and maintaining District records. In more recent years, many of these day-to-day activities have shifted to and are being performed by the District's contractors.
- In May 2016, the District contracted with a law firm to provide legal counsel and, in 2018, expanded the scope of work to include activities such as certifying assessment rolls, preparing lien packages, and processing and accounting for program administration fees.
- In 2018, the District contracted with two accounting firms to provide accounting services and handle activities such as processing and recording transactions, reconciling financial activity, and preparing financial reports.

Using contractors is a reasonable approach to ensuring the District's capacity to carry out its operational responsibilities. However, as the District grows and matures and its workload increases in scale, scope, and complexity, the District's de facto management structure will be difficult to maintain over the long term. For example:

- In organizations that rely on a combined board chair-chief executive/administrator model, the governing board is limited in its ability to effectively hold the chief executive accountable for operations when they are also the board's chair.
- The District relies heavily on third-party contractors for District operations and the administration of the C-PACE Program. However, use of third-party contractors still requires ongoing coordination and monitoring by District management to ensure that the Program Administrator and other service

providers working under contract adhere to established policies and procedures, comply with relevant contract provisions, and meet performance expectations. As the workload of the District's operations and programs increases, it is unlikely that the Board or the Board Chair will be able to continue directly monitoring the activities of the Program Administrator or its other third-party providers.

- Board members are not compensated for their services [Section 32-20-104(2)(d), C.R.S.]. It is unreasonable to expect that the District's management function will continue to fall to one or more of its volunteer Board members.

If management is responsible for the design, implementation, and operating effectiveness of the District's system of internal control, then the District's system of internal control cannot be fully operational and effective without a formally defined management structure. Additionally, the Board cannot fully exercise its governance role and responsibilities unless the District's management is separate from the Board. The Board needs to formalize the District's management structure, including clearly defining the scope, authority, and responsibilities of a chief executive/administrator position that is separate from the Board. Overall, the District's chief executive/administrator—whether an employee of the District or another independent contractor—should report directly to the Board and be responsible for the day-to-day management, coordination, and administration of the District's operations and programs within the overall strategic direction and policy objectives established by the Board.

### **Relationship with CEO**

Since its inception, the District has had a close relationship with CEO. CEO has provided leadership through its designee on the Board; CEO has provided the bulk of the District's funding to date through grants to the District; the District's Recording Secretary, who is appointed by the Board, is a CEO employee; the District's business office established in the District's bylaws is CEO's physical office location; and general administrative information about the District (i.e., Board members' names; Board meeting agendas, materials, and minutes; and approved budgets) is hosted on CEO's website as part of the "www.colorado.gov" domain.

However, the District's ongoing reliance on the CEO-designated Board member and other CEO staff and resources for operational support contributes to a lack of clarity about the relationship between the District and CEO. The District should not be in a position where the intended administrative separation between the District and the State outlined in statute is in question. Moreover, we found that:

- CEO includes the C-PACE Program in its annual performance plan under the SMART Government Act [Section 2-7-201, et seq., C.R.S.] and incorrectly states that “CEO has **developed and continues to oversee**...[the] Property Assessed Clean Energy (C-PACE) [Program] (emphasis added).” Although CEO staff are involved in the C-PACE Program in their official capacity as District representatives, CEO’s SMART Government Act-related documents do not acknowledge that the District—not CEO—is the governing entity that is statutorily responsible for the development, management, and oversight of the C-PACE Program.
- To date, the District has received \$1.335 million in start-up grant funding from CEO. It is reasonable that CEO would be a source of grant funding for the District given both organizations’ common policy goals of promoting energy efficiency and renewable energy improvements. However, we reviewed the 2016, 2017, and 2019 grant agreements between CEO and the District and found that the same individual was listed as the principal agent on behalf of CEO as the granting agency and on behalf of the District as the grantee. At a minimum, acting as the principal representative for both the grantor and the grantee presents the appearance of a conflict of interest, as well as uncertainty about which organization’s interests the individual would represent.

The District’s ongoing reliance on CEO staff and resources also may not be sustainable on a long-term basis given the potential for changes to occur at CEO. For example, a future CEO Director could choose only to maintain their or their designee’s involvement in the District’s activities as a Board member. As mentioned previously, the District relies on CEO for operational support in several areas. We note that as recently as 2017, there were significant debates during the State’s budget process about whether CEO’s operating budget would be authorized for another year. The District should ensure that it is as insulated as possible from the effects of changes in the scope, scale, or programmatic direction of CEO’s activities that could occur.

CEO has played a critical and valuable role in the District’s early formation and development, and the District may benefit from continued support from CEO. However, statute establishes the District as a separate legal entity that is not an agency of state government nor subject to administrative direction by any department, commission, board, or agency of the State. To the extent that the District’s Board continues to rely upon CEO staff and resources to support the District’s operations, the scope of these services, responsibilities, and related compensation should be clearly outlined in a formal intergovernmental agreement or memorandum of understanding between the District and CEO.

## **Recommendation No. 2:**

The Board of Directors for the Colorado New Energy Improvement District (District) should ensure the sustainability of the District and its activities and programs by formally establishing the District's management structure, including clearly defining the scope, authority, and responsibilities of a chief executive/administrator position that is separate from and accountable to the Board.

### **District Board Response:**

Agree. Implementation Date: December 2021.

The Board agrees that taking additional steps to formalize the District's management structure is an important goal. In 2018 and 2019 commensurate with an increase in project closings, it became cost effective to shift numerous duties previously performed by the CEO board member to general counsel and a CPA firm in an effort to professionalize functions and prepare for the future. The Board believes that the sustainability and long-term competitiveness of the C-PACE Program will be dependent on the Board's ability to continue to delegate project-specific administration activities and assessment support services to the program administrator, a District manager, and other third-party consultants. The Board agrees that creating a separate chief executive/administrator position with a clearly defined scope of work, authority, and responsibilities who reports directly to the Board is in our long-term interest and we will work toward this outcome. As part of implementing this recommendation, the Board will begin by scoping the potential chief executive/administrator position by December 2019. Creating that position may also require restructuring the functions currently performed by the District's existing contractors and program administrator. The Board will then analyze the financial viability during its annual budgeting process to ensure that the addition of this position does not impede progress on the District's financial self-sustainability goal in the near term. Provided that all of this interim work goes as planned, we expect that full implementation of the recommendation will occur by December 2021.

## **Recommendation No. 3:**

The Board of Directors for the Colorado New Energy Improvement District (District) should ensure clarity of administrative separation between the District and the State by executing a formal intergovernmental agreement or memorandum of understanding with the Colorado Energy Office (CEO) that outlines the scope of services, responsibilities, and related compensation for any activities within the scope of the District's statutory authority that are performed, provided, or supported by CEO employees or resources.

## **District Board Response:**

Agree. Implementation Date: December 2019.

The Board agrees that to the extent that the District continues to rely on the CEO personnel to provide administrative support, including the Board seat filled by the CEO Executive Director (or his or her designee), the District will formalize those expectations with the CEO through an intergovernmental agreement (“IGA”) or memorandum of understanding (“MOU”) with the State of Colorado/CEO. The IGA or MOU will set forth the specific scope of services, responsibilities, and any related compensation for administrative support activities to be provided by CEO employees, and would, in the Board's view, set clear expectations regarding the deliverables to be provided to the District by the CEO. In addition, the IGA or MOU may be revisited and amended by the parties, on an as-needed basis, as the level of services or responsibilities of the CEO changes over time.