State of Colorado
Colorado Office of the State Auditor

Performance Audit of the Colorado New Energy Improvement District

March 2024

455 Capitol Mall • Suite 700 • Sacramento, California • 95814 • Tel 916.443.1300 • www.secteam.com

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REPORT NUMBER 2355P

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March 15, 2024

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,

George Skiles, Partner
Sjoberg Evashenk Consulting, Inc.

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Report Highlights

Colorado New Energy Improvement District

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Key Concern

The Colorado New Energy Improvement District (District) does not appear to be a financially sustainable organization independent of state government, as required by statute. The District has been unable to maintain a positive cash flow through program fees since it approved its first project in 2016 and continues to rely on state grants and staffing support from the Colorado Energy Office (CEO) to continue operations. In addition, the District's Commercial Property Assessed Clean Energy (C-PACE) Program has experienced stagnating or declining performance over the last few years.

Key Findings

- The District is intended to operate independently of the State and to generate revenue through fees and/or bond financing. It has not issued bonds, but its revenues have not been sufficient to support its operations.
- Without state grants, the District would have had a negative cash flow every year since 2016, when it approved its first project. Despite receiving more than $2 million in grant funds, the District has operated with a negative cash balance in 4 of the last 8 years.
- The District's primary source of self-generated revenue is its program administration fee, but it has not set fees to ensure sustainability. The District has not determined the true cost of funding its operations, set fees consistent with these costs, or passed on all relevant costs to property owners. In addition, the District has not fully analyzed its fee structure to determine what, if any, adjustments could be made to improve its financial sustainability.
- Over the last 8 years, the District has split its program administration fee with the program administrator, which ranged from 10-90 percent to 17-83 percent splits, with the program administrator receiving the bulk of the revenue. This commission-based compensation model created the inherent risks that the program administrator could be compensated in a manner that exceeds its true cost of operations, and/or that it may not receive enough funding to cover basic operating needs. With the District operating with a negative cash flow, neither outcome is desirable.
- Key performance indicators show that the C-PACE program has become less effective in recent years, with the number of projects declining every year since 2019, and corresponding declines in the economic and environmental benefits C-PACE projects produce. For example, in 2023 the District closed 10 projects, the lowest number of projects closed since 2017. These declines translate to less efficient program operations, such as increased costs per closed project.

Background

- The District is responsible for the success of the C-PACE Program, which allows commercial property owners to obtain financing for energy efficiency or renewable energy projects with loans that are secured and paid for through a special assessment and corresponding lien that the District places on the property.
- Between 2016 and 2023, the District closed a total of 126 projects totaling approximately $256 million through the C-PACE Program.
- As of December 31, 2023, 39 of Colorado's 64 counties authorized participation in the C-PACE Program, although C-PACE projects have only been approved or completed in 24 of those counties.
- The District is governed by a seven-member Board of Directors that includes the Director of the CEO, or his or her designee, and six other members appointed by the Governor.

Recommendations Made

9

Responses

Agree: **9**

Partially Agree: **0**

Disagree: **0**

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Introduction & Background

The Colorado New Energy Improvement District (District) is a statewide special statutory district created in 2010 through the enactment of the New Energy Jobs Creation Act of 2010 (House Bill 10-1328). The District was created to establish, develop, finance, and administer a new energy improvement program, called the Colorado Commercial Property Assessed Clean Energy (C-PACE) Program, which encourages eligible real commercial property owners to invest in energy efficiency or renewable energy improvements to their property. The C-PACE Program began operating in 2015, following several legislative changes that are discussed in the Key Legislative History section below, and the District approved its first C-PACE project in 2016.

Property Assessed Clean Energy (PACE) programs have been implemented in states across the United States to promote investment in energy improvements to commercial and residential properties. 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. 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.

Key Legislative History

The New Energy Jobs Creation Act of 2010 authorized the creation of the District and a statewide *residential* PACE program. However, in July 2010, just after the passage of House Bill 10-1328, the Federal Housing Finance Agency issued a statement advising Fannie May and Freddie Mac to avoid buying residential mortgages with PACE assessments because most PACE loans were senior to the mortgage obligations themselves; this would have meant that, in the event of default by the homeowner, the PACE loans would have been paid first by a home sale rather than the outstanding mortgage balance. This statement effectively stalled the development of residential PACE programs nationwide, including Colorado's. Consequently, Senate Bill 13-212 (the New Energy Jobs Act of 2013) expanded the scope of the District and refocused the PACE program on improvements to *commercial* properties. Senate Bill 13-212 also expanded the allowable energy improvements, developed a process to fund new energy improvements through private third-party financing (in addition to special assessment bonds issued by the District), and ensured the consent of mortgage holders to subordinate the priority of their mortgages to the PACE lien (meaning that, in the event of a default, the PACE lien would be entitled to be repaid first). While the District has explored potential models of residential PACE programs, federal guidelines around PACE financing generally have not changed, effectively continuing to limit options for states to pursue residential PACE financing programs. As of December 2023, the District only operated a commercial PACE program and had not implemented a residential PACE program.

In March 2023, the Governor signed House Bill 23-1005, which further expanded allowable energy improvements to include "resiliency" improvements such as installations or modifications that improve a property's structural integrity for seismic events; indoor air quality; ability to withstand wind, fire, flooding, or

electrical power outages; or ability to mitigate the effects of extreme temperatures and other environmental hazards. House Bill 23-1005 also added "water efficiency" projects (e.g., those that reduce water consumption or conserve water on the property) as allowable improvements.

Colorado New Energy Improvement District

According to statute, 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.]. According to testimony during committee of reference hearings for the District's enabling legislation, the District was created because the Colorado Constitution gives "special improvement districts" the ability to levy assessments on real property in order to generate revenue to fund improvements that benefit the public, including energy efficiency. The District is governed by a seven-member board of directors (Board) that includes the Director of the Colorado Energy Office (CEO) or their designee and six additional members, appointed by the Governor for 4-year terms, who collectively represent or have executive-level experience in commercial or residential real estate development, financial institutions, and the utility industry, as well as representatives of the energy efficiency and renewable energy industries [Section 32-20-104(2)(a)(II), C.R.S.]. Board members receive no compensation for their services but are entitled to reimbursement of necessary expenses (e.g., travel and lodging) incurred in the discharge of their official duties.

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 C-PACE Program *and* whose property is located within those counties where the county commission has adopted a resolution authorizing the District to operate the C-PACE Program within its jurisdiction.

Colorado Commercial Property Assessed Clean Energy Program

In the legislative declaration establishing the District and authorizing Colorado's C-PACE Program [Section 32-20-102(1), C.R.S.], the General Assembly states that "it is in the best interest of the state and its citizens and a public purpose to enable and encourage the owners of eligible real property to invest in new energy improvements, including energy efficiency improvements and renewable energy improvements." The General Assembly further outlined that new energy improvements, including energy efficiency improvements and renewable energy improvements, will help to:

- Protect owners of eligible real property from the financial impact of the rising cost of electricity produced from nonrenewable fuels,
- Promote informed choices and maximize the benefits of the program for both individual owners of eligible real property and society as a whole,
- Improve air quality and may help to mitigate climate change (due to reductions in the amount of emissions of greenhouse gases and environmental pollutants resulting from decreased use of traditional nonrenewable fuels),
- Increase the value of the eligible real property improved,

- Create jobs and stimulate the economy by (1) directly creating jobs for contractors and other persons who complete new energy improvements, and (2) reinforcing the leadership role of the State in the Colorado energy economy, thereby attracting new energy manufacturing facilities and related jobs to the state, and

- Provide a meaningful, practical opportunity for average citizens to take action that will benefit their personal finances and the economy of the state, promote their own and the nation's energy independence and security, and help sustain the environment [Section 32-20-102(1)(a), C.R.S.].

The C-PACE Program allows owners of existing commercial or multifamily buildings (i.e., five or more units) or new commercial construction to finance qualifying improvements, including:

- Energy efficiency improvements, which are installations or modifications that are designed to reduce energy and/or water consumption, such as insulation; window and door improvements; automatic energy control systems; heating, ventilating, or air conditioning and distribution systems; caulking and weather-stripping; lighting fixtures and controls; energy recovery systems; daylighting systems; combined heat and power (CHP) and waste-to-power projects; electric vehicle charging equipment; and other modification, installation, or remodeling approved as a utility cost-savings measure by the District.

- Renewable energy improvements, which 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).

The Colorado C-PACE Program allows an eligible commercial property owner to finance the large, up-front cost of energy or other eligible improvements on a property through a loan and then pay the costs back over a period of time, which can be as long as 25 years. Financing is provided by third-party capital providers, such as banks and other commercial lenders. 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. 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. All qualified and approved capital providers are eligible to provide C-PACE financing.

C-PACE financing is intended to offer terms that may be more attractive and accessible than other financing options. For instance, there is no maximum financing amount available through the C-PACE Program for improvements to existing properties, whereas there may be limits that lenders impose on more traditional financing alternatives. However, as of December 31, 2023, the financing amount available for improvements to newly constructed properties cannot exceed 35 percent of the total eligible construction cost. Other benefits to C-PACE financing could include lower interest rates because a C-PACE loan may present less risk to lenders since the C-PACE lien is placed in a priority position over other lienholders, and longer terms (up to 25 years), which translates to lower annual payments. C-PACE financing also benefits commercial property owners because, while traditional financing for energy efficiency projects requires property owners to bear the burden of the cost of the improvements while the tenants that occupy the properties and pay utility bills benefit from the improvements, C-PACE financing incentivizes property owners to invest in energy efficiency

projects by allowing the cost of the improvements to be passed on to the tenant that benefits from the enhanced energy efficiency.

Participation in the C-PACE Program, and the assessment of a C-PACE lien on one's property, is voluntary and requires that the property owner submit an application to the District, adhere to eligibility criteria, and agree to the placement of the lien on the property. 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 special 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.

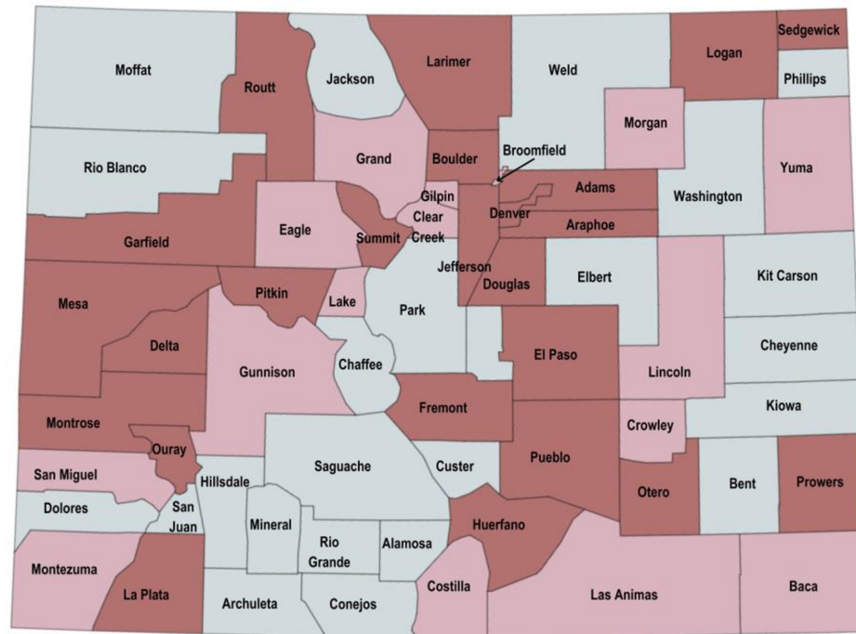
Repayment of the loan is made through a special assessment that the District levies against the property based on the cost of the improvements, financing, and related expenses (e.g., energy audits, legal expenses, appraisals, title insurance, etc.). The District places a lien on the property until the loan is repaid.

Each county that participates in the Program enters into an intergovernmental agreement with the District and takes on responsibility to collect the C-PACE assessments from participating property owners via the 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. Statute authorizes county treasurers to collect a service fee equal to 1 percent of the amount of each special assessment payment to support these activities [Sections 32-20-105(3) and 30-1-102(1)(c), C.R.S.]. This fee is included in the total special assessment amount placed on the county's property tax rolls, and is reflected as District revenue that is passed on to the counties. The assessment is not considered a property tax even though the loan payments are collected through the property tax collection system. Counties remit funds to the District (or its designated fiduciary), net of the 1 percent statutory county service fee noted above, for distribution to the third-party capital providers that provide funding for the projects.

Because the C-PACE assessment lien is a debt of property—tied to the property as opposed to the property owner—the repayment obligation generally transfers with property ownership if the property is sold prior to the end of the agreed-upon special assessment period. However, a property owner may satisfy the repayment obligation in advance, at which time the District's assessment lien is released from the subject property. 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 [Section 32-20-107(4), C.R.S.]. The District does not have the authority to file a civil action of foreclosure on the subject property.

As of December 31, 2023, the District reported that it has assisted eligible property owners obtain funding through third-party capital provider financing for 126 projects, with financing totaling almost $256 million, since the C-PACE Program began securing financing in 2016. As of December 31, 2023, 39 of Colorado's 64 counties authorized such participation, although C-PACE projects have only been approved or completed in 24 of those counties. These counties are highlighted in Exhibit 1.

EXHIBIT 1. MAP OF COLORADO COUNTIES PARTICIPATING IN THE DISTRICT'S C-PACE PROGRAM



Counties authorized to participate in C-PACE | Counties authorized to participate in C-PACE and in which C-PACE projects have been approved

Source: C-PACE Website, Program Impact Statements Provided by CNEID

Program Administration

To administer the C-PACE Program, the Board of Directors has authority 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 contract for professional services, such as a program administrator [Section 32-20-105(2)(j)(I), C.R.S.]. Since the District was created, it has not hired any employees, but has instead entered into a memorandum of agreement with the CEO, an agency within the Governor's Office, for a CEO staff person to serve as the Board's recording secretary and perform District management functions. According to the memorandum of understanding, this includes reporting to the Board regarding District operations, handling procurement and regular management of the District's professional services agreements, representing the District with the public and program participants, and assisting with development of the District's annual budget, among other things.

The District has contracted with a professional services firm, Sustainable Real Estate Solutions, Inc. (SRS), to serve as the program administrator with responsibility for the day-to-day coordination and delivery of the C-PACE Program in accordance with the Program Guide adopted by the Board. This program administrator has administered C-PACE programs in other states as well, including Connecticut, Nevada, Rhode Island, Utah, and Virginia. The District first contracted with SRS in 2015, executed a second contract in 2018, and extended the term of that contract through eight amendments until June 30, 2024. Payments to the program administrator represent the District's single largest operating expense item, as illustrated in Exhibit 5, and totaled $210,000 in Calendar Year 2023.

The District also contracts with other private firms, including law firms, accounting firms, and others to provide routine and ad hoc services to the District and help coordinate various services for and on behalf of the District.

Under statute [Sections 32-20-105(3) and 32-20-106(4), C.R.S.], the District's administrative duties include:

- Marketing the program to owners of eligible real property,
- Managing an application process for property owners wishing to participate in the program,
- Ensuring that mortgage holder consent is obtained for all eligible real property participating in the program to subordinate the priority of such mortgages to the C-PACE lien,
- Certifying contractors to construct or install new energy improvements,
- Tracking and preparing annual reports on the following program metrics: (1) quality of new energy improvements for which the District has made reimbursement or a direct payment, if deemed necessary by the Board; (2) total energy savings achieved; (3) number of program participants; (4) total amount paid to contractors; (5) number of jobs created; (6) number of defaults by program participants and total losses therefrom; and (7) total amount of bonds the District has issued, as authorized by Section 32-20-105(3)(g), C.R.S., and
- Preparing district special assessment rolls for county treasurers in each county with C-PACE projects each year.

The program administrator's contractual responsibilities to the District fall into three primary areas:

- Program management—this includes creating and maintaining the District's website and all informational program materials, managing project application intake and processing, ensuring project eligibility, pre-qualifying all C-PACE contractors, and maintaining regular communication with the District.
- Marketing activities—this includes managing education and outreach campaigns for property owners, capital providers, contractors, utilities, and counties; preparing case studies; addressing questions from potential program applicants; and preparing press releases for newly closed projects.
- Key aspects of the District's financial management—this includes managing capital provider application processes, supporting capital providers during the financial transaction closing process, coordinating county activities and relationships, assisting county assessors and treasurers with setting up special assessments, assisting the District with certification and transmission of assessment rolls to county treasurers, and coordinating the exercise of remedies on default.

District & Program Funding

Because the District does not have general taxing authority [Section 32-20-102(2)(a)(I), C.R.S.], it relies on administrative fees charged to participating property owners and grants provided by the CEO to provide funding to pay for its operations costs.

The District has historically charged a one-time program administration fee for each unit of eligible real property assessed. The program administration fee is typically included in the total financed amount for the project and is only due in the event of successful project financing. The amount of the fee is variable and has been modified a few times since the District's contract with the program administrator was executed in 2015. Specifically,

- Between 2015 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. Through 2017, the full amount of this fee was paid to the program administrator as compensation for administering the C-PACE Program. Starting in January 2018, the District began retaining 10 percent of the fee for its costs (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 fee amount 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.

- Beginning in February 2020, the program administration fee was changed to 2.25 percent of the total financed project amount, with a $5,000 to $50,000 minimum-maximum fee range. The District retained the greater of 17 percent or $2,500 of the fee amount, and the remaining fee amount went to the program administrator. For example, if 2.25 percent of the total financed amount for the project was less than $5,000, the program administration fee was set at the $5,000 minimum amount; if 2.25 percent of the total financed amount for the project was more than $50,000, the program administration fee was capped at $50,000. If a project involved multiple eligible units of real property, the minimum program administration fee was adjusted to ensure that it did not exceed 2.25 percent of the total amount financed for the project or the maximum program administration fee of $50,000, whichever was less. These changes were made in an effort to encourage new projects, while also generating sufficient annual revenues to support the District's operations.

- In August 2023, the District modified its fee structure to reflect the pre-pandemic cap of $75,000 and post-pandemic method of allocating fee revenue between the program administrator and the District. This structure is reflected in Exhibit 2.

EXHIBIT 2. PROGRAM ADMINISTRATION FEES AS OF AUGUST 7, 2023

Total Project Amount	Administration Fee	Allocated Share	
		District	Program Administrator
Up to $200,000	$5,000	$2,500	$2,500
$200,000 to $585,235[1]	2.5%	$2,500	2.5% less $2,500
$585,236 to $2,999,999	2.5%	17% of Fee	83% of Fee
$3,000,000+	$75,000	$12,750	$62,250

Source: Contract between the District and the program administrator to provide program administration services

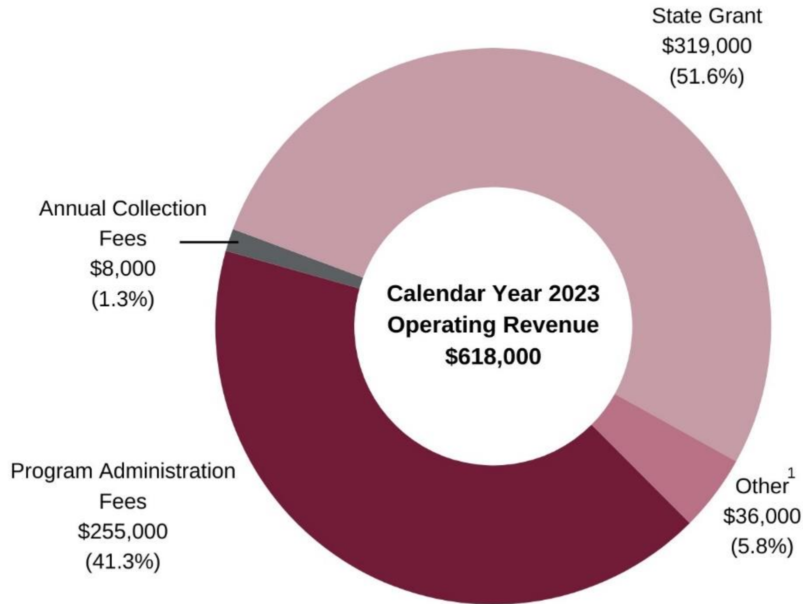
Note: [1] $585,235 is the point at which the District would receive $2,500 under the 17 percent / 83 percent allocation of the fee to the District and program administrator, respectively.

Separate from the one-time program administration fee charged to projects, the District also began to impose an annual collection fee, or loan servicing fee, of $100 for projects that closed on or after February 1, 2020. The implementation of this fee was initiated in response to the Office of the State Auditor's (OSA) 2019 audit of the District, which found that the program administration fee alone may not be sufficient to ensure sustained funding to service lien collections over the course of 25 years. This annual collection fee is incorporated into the special assessment charged against the property through property tax rolls. On July 1, 2022, the District modified the annual collection fee for all projects closed on or after July 2022, and there is now a tiered fee structure that is based on the total amount financed to fund the improvement project, as follows.

Total Project Amount/Financed Amount	Annual Collection Fee
Up to $1,000,000	$250
$1,000,000.01 to $2,000,000	$500
$2,000,000.01 to $3,000,000	$750
$3,000,000.01+	$1,000

In addition to these two program fees, the District has historically received grant funding through the CEO. For example, the CEO provided $319,000 to the District in 2023, which accounted for 52 percent of the District's operating revenue that year. As illustrated in Exhibit 3, District operating revenue for Calendar Year 2023 reached $618,000, which did not include special assessment monies collected on behalf of capital providers or counties.

EXHIBIT 3. PRIMARY REVENUE SOURCES, CALENDAR YEAR 2023 (UNAUDITED)



Source: The District's 2023 unaudited financial statements

Note: [1] "Other" includes revenues from project deposits, hearing continuances, release of lien fees, filing fee reimbursement, and interest income.

Audit Scope and Methodology

The Colorado Office of the State Auditor (OSA) 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 5 years. Audit work was performed from August 2023 through February 2024. 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, Board meeting agendas and minutes, historical legislative records relating to the enabling legislation of the District and C-PACE Program, and District financial records, grant agreements, and contracts.

- Interviewed six of the seven District Board members (one Board member did not respond to interview requests), including the Board chair, an employee of the CEO, the District's Recording Secretary (also an employee of the CEO), and the C-PACE program administrator.

- Evaluated District revenue and expenditure data, adopted budgets, project and revenue forecasts, audited financial statements, and other financial information.

- Evaluated performance metrics and workload indicators for the C-PACE Program, which included reviewing records for a nonstatistical sample of 10 C-PACE projects that were closed between 2019 and 2022. These 10 projects were selected to include a range of new construction, retrofit, and retroactive retrofit projects; projects located in various counties; different project types (e.g., insulation, solar, lighting, or a combination of measures); and a range of small ($75,000) to large ($55 million) amounts financed. The results of our sampling cannot be projected to the population of all C-PACE projects. However, the sample results are valid for confirming whether the projects complied with statutory requirements and procedures established in the District's Program Guide, and, along with the other audit work performed, provide sufficient, reliable evidence as the basis for our findings, conclusions, and recommendations.

- Interviewed administrators of statewide C-PACE programs operating in five other states, including Minnesota, Connecticut, Texas, Rhode Island, and Michigan, and researched the practices of an additional eight statewide programs, including Utah, Nebraska, New York, Oregon, Ohio, Montana, Florida, and California, which included obtaining information regarding their organizational structures, funding sources, program design, and performance.

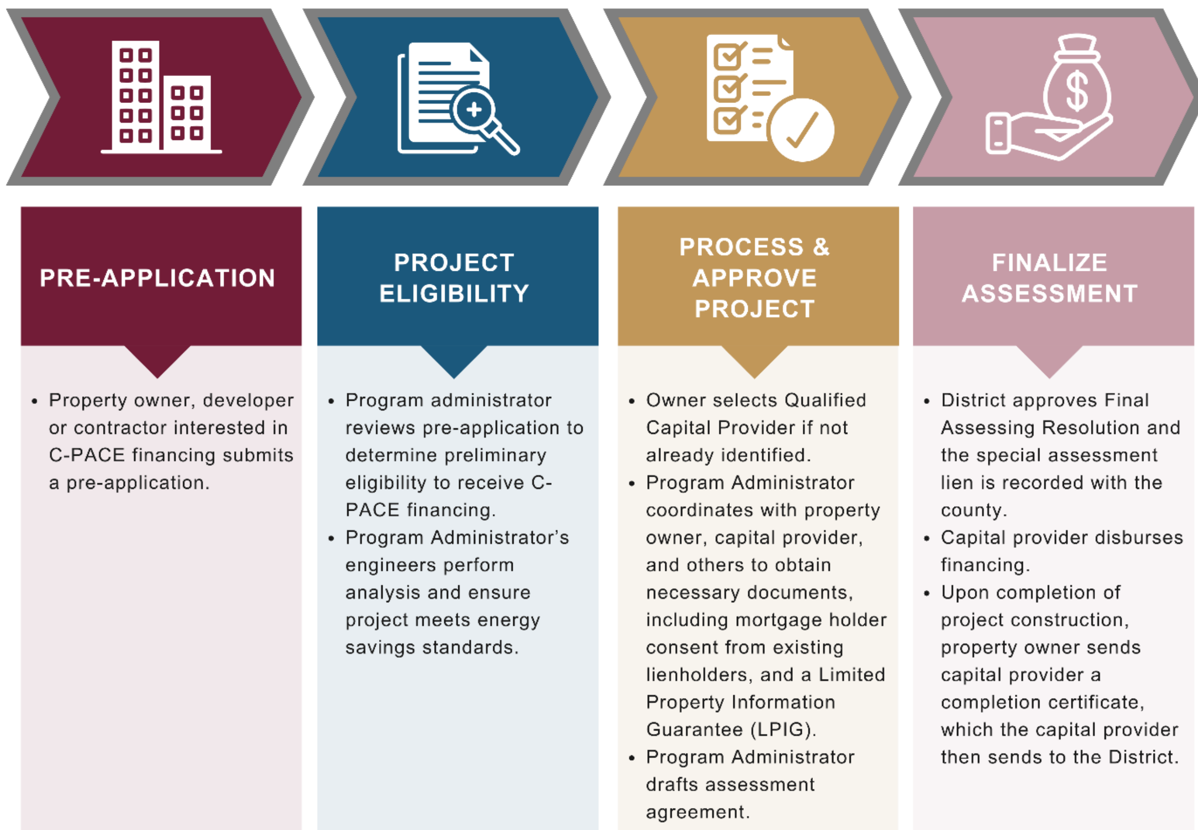
As required by auditing standards, we planned our audit work to assess the effectiveness of those internal controls that were significant to our audit objectives. Details about the audit work supporting our findings and conclusions, including any deficiencies in internal control that were significant to our audit objectives, are described in the remainder of this report.

A draft of this report was reviewed by the District and the Board. Obtaining the views of responsible officials is an important part of ensuring that the report is accurate, complete, and objective. Sjoberg Evashenk Consulting, in consultation with the OSA, were solely responsible for determining whether and how to revise the report, if appropriate, based on the Board's comments. The written responses to the recommendations and the related implementation dates were the sole responsibility of the Board.

Finding 1 – Financial Sustainability

The District provides a singular service; it implemented the C-PACE Program to provide commercial property owners access to alternative financing options with the chief goals of benefiting the environment and the economy. Achieving this purpose requires the District to establish core business processes that include marketing the program and ensuring counties, contractors, capital providers, and property owners are familiar with the C-PACE Program. Statute also requires the District to develop an intake process to review and vet potential projects; ensure the eligibility and feasibility of projects; facilitate the private funding of approved projects; and verify compliance of applicants, contractors, and capital providers. The District contracted with its program administrator to perform this work. Specifically, the program administrator established a process flow, a summary of which is illustrated in Exhibit 4, for vetting potential projects prior to the Board's approval.

EXHIBIT 4. C-PACE PROJECT REVIEW AND APPROVAL PROCESS



Source: Summary of the C-PACE Program Guide prepared by Sjoberg Evashenk Consulting

In addition to developing an intake process, the District, like any enterprise, must establish a management and administrative structure to support, monitor, and ensure the success and compliance of program operations. This includes providing contract oversight and monitoring, general bookkeeping and accounting functions, reviewing and approving District expenditures, and providing sound legal counsel, among other administrative support functions.

Management, program, and support activities must be well established and appropriately funded for the District, or any enterprise, to succeed over the long term.

What audit work was performed and what was the purpose?

We reviewed relevant statutes, District bylaws, historical legislative records, District financial records, grant agreements, and contracts; interviewed District board members, contractors, and CEO representatives; identified trends in operating expenditures, revenues, and cash flow over the 8-year period beginning in 2016, when the District approved its first project, through December 2023, and analyzed revenue sources in the context of financial sustainability. The purpose of the audit work was to determine the extent to which the District appears to be financially sustainable.

How were the results of the audit work measured?

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.]. It is a special district of the State of Colorado, subject to bylaws adopted by an independent Board of Directors [Sections 32-20-105(2)(c) and 32-20-104(2)(a), C.R.S.], and it is intended to have perpetual existence [Section 32-20-105(2)(a), C.R.S.]. Therefore, as a special district with the obligation to sustain ongoing operations [Sections 32-20-105(2)(a) and 32-20-106(4), C.R.S.], it is incumbent upon the District to establish a financing and administrative structure designed to ensure long-term sustainability.

Statute requires the District to set an annual budget [Section 32-20-105(2)(d), C.R.S.], which should provide realistic data on how much revenue the District needs and how much money the District expects to spend to finance a new energy improvement program through the following funding mechanisms.

- <u>Fees</u>—Statute states that "the [D]istrict may charge program application fees" [Section 32-20-105(3), C.R.S.]. 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 program. In addition, for projects closed on or after February 1, 2020, the District began imposing an annual $100 loan servicing fee; this fee was modified in 2022 to establish a tiered model that requires larger projects to pay a higher loan servicing fee, as noted in the background section of this report.

- <u>Special assessments</u>—Statute authorizes the District to "levy special assessments against eligible real property specially benefited by a new energy improvement based on the cost to the district of the new energy improvement" [Section 32-20-106(3)(a), C.R.S.]. Special assessments are not based on the assessed value of the property, but rather, they may represent annual charges for services, improvement district charges, local district or other voter-approved special taxes, special benefit assessments, and fees.

  Modeled after improvement districts within Colorado, the District uses special assessments as its method of collecting loan payments on behalf of third-party capital providers. Special assessments are considered "pass-through revenue" for the District because borrowers who obtain financing from

capital providers for new energy improvements make payments to county treasurers who then remit that money to the District to pass on to the lenders; the District also retains a portion of the assessment amount to help recover its costs related to the project.

- Bonds—Statute states that "the [D]istrict shall issue special assessment bonds in an aggregate principal amount of not more than $800 million for the purpose of generating the moneys needed to make reimbursement or a direct payment to district members and to pay other costs of the district" [Section 32-20-108(1), C.R.S.].

  The District is also required to arrange for an appropriate loss reserve in order to obtain the necessary bond rating. [Section 32-20-105(4), C.R.S.]. Statute requires the District to fund a loss reserve in order to pay the special assessment on a property in the event the property owner defaults on a property tax payment [Section 32-20-107(4)(g), C.R.S.]. This protects capital providers (where third-party financing is used) and the District (where bond financing is used) in the event of default.

- Grants—Statute authorizes the District to apply for and accept grants [Section 32-20-105(2)(l), C.R.S.].

What problem did the audit work identify?

Overall, the District does not appear to be a financially sustainable organization independent of state government, as required by statute. Instead, the State has, since the District's inception in 2010, supported District operations both financially and with staffing resources. Without the State's support, the District could not maintain the C-PACE Program.

Financial Resources

The District's financial records indicate its ongoing reliance on CEO grants since 2016, when the District funded its first project, and the District would have had a negative cash flow every year since then if it had not received grant funds from the CEO. Specifically, as of December 31, 2023, the District has relied on grants from the CEO totaling more than $2 million, which provided seed funding for the start-up of the C-PACE Program and supported ongoing District operations. In February 2016, the District was awarded a $735,000 grant, which it used to launch the C-PACE 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, which was intended to enable the District to build a loss reserve pursuant to statute [Section 32-20-105(4), C.R.S.] and to address potential defaults [Section 32-20-107(4)(g), C.R.S.]. The District used $300,000 to establish a loss reserve and, in January 2019, the District returned the remaining $200,000 from this second grant. However, later that same year, the CEO awarded a third grant totaling $300,000 to help pay the District's administrative expenses. While this funding has not been sufficient to ensure consistently positive operating cash flow, it has enabled the District to maintain a positive year-end loss reserve fund balance since 2016.

Despite receiving more than $2 million in grant funds between 2016 and 2023, the District operated with a negative cash flow during Calendar Years 2018 through 2021 and had to use funds from its loss reserve fund balance to pay for day-to-day operating expenses during this period. This is highlighted in Exhibit 5. Most

recently, in 2021, the CEO awarded the District a $1.2 million grant that will fund District operations in annual amounts ranging between $200,000 and $400,000 through June 2025. The purpose of the grant was to help replenish the District's loss reserve and cover the District's administrative and operating expenses until the District "achieves financial self-sustainability through the fee-for-service model." While the CEO has awarded the District sufficient grant funds to support the C-PACE Program, the District is not entitled to receive grant monies indefinitely, and there is no guarantee of if or how much grant funding will be approved in the coming years.

Exhibit 5 provides data on the District's revenues and expenditures, cash flows, and loss reserves for Calendar Years 2016–2023.

EXHIBIT 5. DISTRICT REVENUE AND EXPENDITURES, CALENDAR YEARS 2016–2023

	Calendar Year							
	2016	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**
Revenues	**$738,000**	**$711,000**	**$850,000**	**$3,051,000**	**$4,325,000**	**$5,489,000**	**$8,234,000**	**$9,498,000**
Grants	$735,000	$500,000	$0	$300,000	$0	$13,000	$141,000	$319,000
Program Administration Fees	$3,000	$167,000	$509,000	$608,000	$559,000	$528,000	$390,000	$255,000
Special Assessment Revenue	$0	$44,000	$341,000	$2,111,000	$3,753,000	$4,898,000	$7,646,000	$8,880,000
Special Assessment District Collection Fee[1]	$0	$0	$0	$0	$0	$900	$4,000	$8,000
Other[2]	$0	$0	$0	$32,000	$13,000	$49,000	$53,000	$36,000
Expenditures	**$458,000**	**$477,000**	**$968,000**	**$3,113,000**	**$4,370,000**	**$5,500,000**	**$8,114,000**	**$9,439,000**
Program Administrator Payments	$392,000	$398,000	$451,000	$517,000	$441,000	$428,000	$310,000	$210,000
Special Assessments Paid to Capital Providers	$0	$44,000	$338,000	$2,090,000	$3,716,000	$4,849,000	$7,570,000	$8,791,000
Special Assessments Paid to Counties	$0	$0	$3,000	$21,000	$37,000	$49,000	$76,000	$89,000
Other District Operations[3]	$66,000	$35,000	$176,000	$485,000	$176,000	$174,000	$158,000	$349,000
Cashflow	**$280,000**	**$234,000**	**($118,000)**	**($62,000)**	**($45,000)**	**($11,000)**	**$120,000**	**$59,000**
Cashflow Without Grant Funds	**($455,000)**	**($266,000)**	**($118,000)**	**($362,000)**	**($45,000)**	**($24,000)**	**($21,000)**	**($260,000)**
Ending Loss Reserve Fund Balance	**$280,000**	**$514,000**	**$396,000**	**$334,000**	**$289,000**	**$278,000**	**$399,000**	**$458,000**

Source: Sjoberg Evashenk Consulting's analysis of District financial data. Dollar amounts are rounded to the nearest thousand dollars.

Notes: [1] The special assessment district collection fee began for new projects approved after July 1, 2020.

[2] Other" includes revenues from project deposits, hearing continuances, release of lien fees, filing fee reimbursement, and interest income.

[3] 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 5 years by the Office of the State Auditor that is paid by the District.

Staffing and Other State Resources

The District does not seem to be operating independently from the State, as required by statute. The CEO fulfills certain management responsibilities of the District, without which the District could not operate effectively and without which the Board could not fulfill its own fiduciary responsibilities. Eleven years after its inception, the District still does not directly employ any personnel, and its budget does not account for the potential cost to employ staff. Instead, the District continues to rely on "in kind" staff support that the CEO provides to the District through a memorandum of agreement. Specifically, the Board's Recording Secretary is a staff member of the CEO who is contractually responsible for handling significant aspects of the District's day-to-day operations, including but not limited to:

- Recording all Board votes and composing a record of the Board's proceedings,
- Assisting the Board in developing the District budget,
- Working with contractors to develop assessment rolls for participating counties, Representing the District before the public and program participants,
- Procurement and management of the District's professional service agreements consistent with Board direction, and
- Reporting to the Board of Directors regarding the above.

In addition, the District's contract with the program administrator requires the CEO to serve as the primary contract manager. In addition to the duties described above, this contract requires the CEO to monitor the program administrator's performance under the contract, to be the primary liaison with the program administrator, and to supervise the performance of any District obligations under the contract. This work is generally performed by the same individual serving as the Board's Recording Secretary. The CEO staff person who serves as the Board's Recording Secretary also has full-time responsibilities with the CEO and reported that while the CEO oversees program administrator activities through bi-weekly meetings, project pipeline reviews, and other as-needed communications, the CEO does not have the resources to oversee all of the program administrator's activities or its compliance with all statutory or programmatic requirements.

In addition to providing direct staff support to the District, the State also hosts the District's website and provides basic web hosting services. The District employs the services of the State's centralized website administrator, the Colorado Statewide Internet Portal Authority, to develop and administer the District's website but does not compensate the State for this service.

Why did the problem occur?

There are several contributing factors for why the District has not been able to achieve financial sustainability and is not operating independently from the State.

- Management Structure—The District's Board of Directors, when drafting its bylaws and establishing the structure of the District, established certain board (e.g., chair and secretary) and non-board officer positions (e.g., district counsel and recording secretary), but never established an executive-level

officer or alternative management structure with specific responsibility for managing the District's operations and finances. Instead, the District contracted with a program administrator to manage the C-PACE program and handle significant activities of the District, as described in the introduction of this report. However, as the C-PACE program evolved and grew, it became apparent to the Board and the CEO that the program administrator was not equipped or empowered to perform activities necessary for the District operations, such as overseeing its own performance, approving District expenditures, and maintaining the District's financial records. The Board, through its bylaws, resolutions, and contracts, assigned such responsibilities to CEO employees and other third-party service providers. Without any other responsible party willing or able to take on these essential duties, and without a formal management structure, the CEO assumed certain management responsibilities of the District and, in so doing, has continued to dedicate resources to District operations during the 11 years since the District began operating the C-PACE program. According to members of the Board, the sustainability of the District remains a priority. The Board has considered and implemented fee adjustments in order to attain sustainability, efforts that have not yet achieved their intended result, and is open to broader structural changes to help the District achieve financial sustainability.

- Fee-Setting Methodology—The District's primary source of self-generated revenue is its program administration fee, but it has not employed a sound methodology in setting this fee. The District's fee-setting approach has not sufficiently accounted for the true cost of funding District operations, nor has the District completed a comprehensive analysis of its fee structure to determine what, if any, adjustments could be made to improve its financial sustainability.

  First, the District's approach for setting its program administration fee was not based on historical revenue trends or reliable revenue projections, nor was it based on realistic expenditure estimates; rather, the fee was based on the program administrator's projections, which were consistently overly optimistic.

  Although the District's revenue and expenditure data show that charging a one-time administrative fee has not resulted in a sustainable revenue stream, between 2018 and 2022, the District tried lowering its fees to generate more business, including lowering the maximum fee to $50,000 and lowering the fee rate from 2.5 percent to 2.25 percent. However, those changes ultimately did not result in more projects.

  Since Calendar Year 2020, the District retains 17 percent of the fee with the remaining 83 percent of the fee going to the program administrator. Since August 2023, the District set the program administration fee at 2.5 percent of the total eligible financed project amount, not to exceed $75,000 per project. However, as shown in Exhibit 6, in Calendar Years 2019 through 2023, the District's share of actual fee revenue was not sufficient to cover the direct costs of its operations and fee revenues fell increasingly short of projections in recent years.

EXHIBIT 6. ACTUAL AND BUDGETED ADMINISTRATIVE FEE REVENUE, OPERATING EXPENSES, AND OPERATING CASH FLOW, CALENDAR YEARS 2019–2023

	Calendar Year				
	2019	**2020**	**2021**	**2022**	**2023**
Administrative Fee Revenues					
Budgeted	$719,000	$1,147,000	$874,000	$763,000	$733,000
Actual Fee Revenue[1]	$608,000	$559,000	$528,000	$390,000	$255,000
Difference	($111,000)	($588,000)	($346,000)	($373,000)	($478,000)
Operating Expenses					
Budgeted	$974,000	$1,147,000	$922,000	$870,000	$857,000
Actual Expenditures	$792,000	$611,000	$578,000	$455,000	$558,000
Difference	($182,000)	($536,000)	($344,000)	($415,000)	($299,000)
Operating Cash Flow					
Budgeted Cash Flow (Budgeted Revenues–Budgeted Expenses)	($255,000)	$0	($48,000)	($107,000)	($124,000)
Actual Cash Flow (Actual Revenues–Actual Expenses)	($184,000)	($52,000)	($50,000)	($65,000)	($303,000)
Additional Amount of Revenue Needed to Achieve Net Zero Cash Flow	$184,000	$52,000	$50,000	$65,000	$303,000

Source: District audited financial statements (2019, 2020, 2021, 2022), unaudited financial statement (2023), and District budget forecasting records

Note: [1] The "Actuals" under "Administrative Fee Revenues" reflect the percentage of the administration fee retained by the District (15 percent for 2019-2021 and 17 percent for 2022-2023).

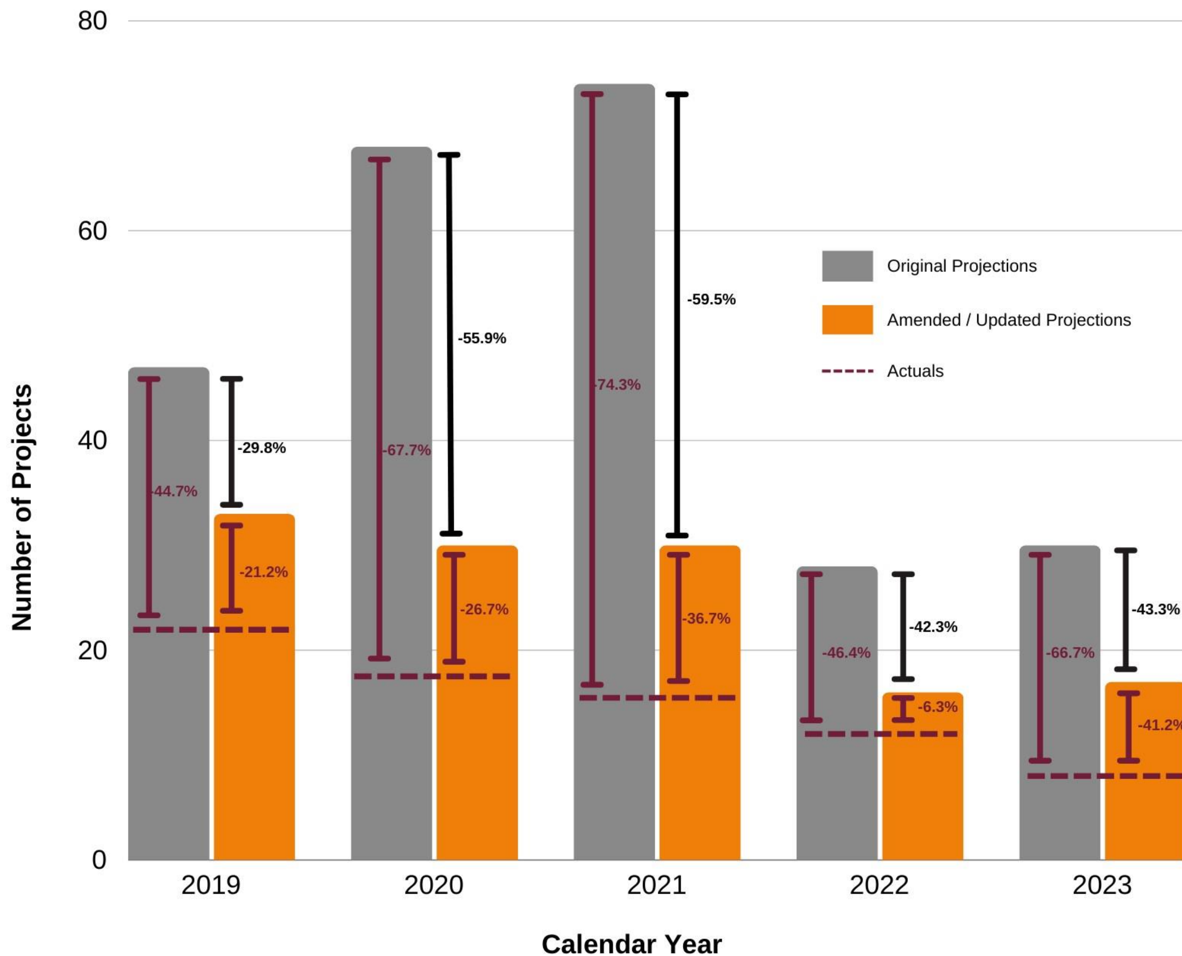
Second, in setting its annual budget, the District has consistently overestimated its project volume, which affects how much fee revenue the District expects to collect. Fundamentally, the District's ability to generate sufficient revenue from the program administration fee—its only source of generated income—is predicated on its ability to attract new property owners and fund new projects. Since its inception, though, the District has not yet achieved the volume of projects projected in its annual budgets. As shown in Exhibit 7, between Calendar Years 2019 and 2023, the number of actual projects funded through the C-PACE Program fell between 44 and 74 percent below the projected amount, which would have ensured the District's sustainability.

According to District management, the program administrator estimates the number of projects it will fund each year based on the pipeline of potential projects known to the program administrator at the time. As previously illustrated in Exhibit 4, interested property owners submit "pre-application" forms to the program administrator when they are interested in obtaining financing through the C-PACE Program. Once preliminary vetting is complete and the project owner is in a position to produce a true estimate of the cost of the improvements, the project is included in the program administrator's listing of potential projects. Based on this listing, the program administrator estimates the number and value of projects that are expected for actual completion and develops budget projections accordingly. The program administrator updates these projections generally around mid-year, or when asked by the District, by reviewing the project pipeline, identifying new projects, removing projects that have fallen through, and estimating which are projected to be approved before year

end. However, this approach is not effective because projections appear speculative and are proven unreliable by historical data.

In the past, the program administrator produced 3-year projections. As recently as 2018 and 2019, the program was receiving more than 200 “pre-applications” per year and was projecting that up to 75 projects a year would participate in the program. However, this level of participation never came to fruition. The most projects ever completed in a year was 26, in 2019—this is described in detail in Finding 2. Exhibit 7 illustrates how initial and revised projections compared to actual project delivery.

EXHIBIT 7: NUMBER OF NEW PROJECTS PROJECTED AND FUNDED, CALENDAR YEARS 2019-2023



Source: Sjoberg Evashenk Consulting generated based on District-provided Program Impact Statements, District Provided Forecasts from 2019-2023

Third, historically, the District only charged a one-time administrative fee at the beginning of each project, rather than ongoing fees that would help cover the District’s costs to provide assessment support services over the life of the existing program assessment liens, which can be up to 25 years. For example, the 10 sampled projects reviewed during the audit had an average lien term of 21 years, ranging from 10 to 25 years. Funding operations through application fees required the District

to attract new applicants and fund new projects at an increasing rate in perpetuity. That is, the District relies on a funding model for the 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 program assessment liens [Section 32-20-106(4), C.R.S.]. Had the District implemented the current tiered annual collection fee schedule in 2016 when it approved its first C-PACE project, the District would have received approximately $157,000 over the ensuing 7 years. While this alone would not have generated sufficient revenue to ensure sustainability, it would have reduced the District's reliance on the State grant funds, and it would have generated a positive cash flow in 2021 and 2022.

In 2020, the District implemented an annual $100 loan servicing fee for new projects and, in 2022, increased this fee to $250 to $1,000 per project per year, depending on the amount financed for the project. In 2023, this resulted in total revenue of $8,000, which did not have a material impact on the District's 2023 negative cash flow (-$260,000). The District's model differs from the model adopted by most other C-PACE programs, which assess loan servicing fees on a point-basis, which means, for instance, that other agencies add 0.25 percent on the interest rate financed through the capital provider. Those agencies use that fee, rather than a flat fee, to fund ongoing operations. While this new fee has not had a material impact on the District's cash flow and does not appear sufficient to have a material impact in the near term, its long-term impact could be substantial to the extent that the District achieves increasing project volume in the coming years.

Fourth, the District has not defined what level of loss reserves would be appropriate to help sustain the District's annual operations, as required by statute. Specifically, statute requires the District to arrange for an appropriate loss reserve in order to obtain the necessary bond rating [Section 32-20-105(4), C.R.S.]. With the assistance of CEO grants, the District has increased its loss reserve nearly 63 percent from $280,000 in Calendar Year 2016, to $458,000 in Calendar Year 2023. The purpose of the loss reserve is to secure an attractive bond rating; a negative cash flow and diminishing loss reserve achieves the opposite.

- Program Administration Cost Structure—There are three key problems with the District's program administration cost structure. First, the revenue sharing arrangement between the District and the program administrator has focused the District's attention primarily on analyzing how to split the percentage of the fee between the District and the program administrator. Their analysis has not taken into consideration what resources are required to complete the duties assigned to the program administrator. There appears to be an emphasis on finding the minimum amount the District needs in the split to cover its expenses, but equal consideration should be given to determining the costs associated with the current duties and expectations of the program administrator. This would give the District information regarding the true cost of core business activities, including how much it would cost for in-house staff to handle those responsibilities. For example, state agencies in Colorado determine the appropriate rate for services by periodically opening a Request for Proposals.

In our review of other statewide C-PACE programs, none of the five agencies we spoke with currently contract with a third-party program administrator; one commented that their program would not be able to accommodate a third-party administrator in its budget. They reported having a small staff of one or two full-time employees leading the day-to-day operations of the program, with a few other part-time or as-needed staff assisting with marketing or providing subject matter expertise. Other states' programs also contract with third parties for other specific responsibilities, such as billing or conducting engineering reviews. The other states charged similar administrative fees, and the three programs run by public or quasi-public agencies were able to operate with a positive cash flow. This evidence suggests that there can be sufficient revenue available from charging fees per project, but the way the District splits its fee revenue is flawed.

Second, the District does not pass the cost of project technical reviews on to the property owner, as other peer agencies do. Each peer agency used the "program administrator" in a manner that was different than the District. Rather than assigning the bulk of the programs' operational responsibilities to a third-party program administrator, each of the other states employed a firm to perform a narrow set of responsibilities related to the technical review of projects, both during the pre-approval and eligibility review process and, sometimes, in the post-construction verification process. This technical reviewer was typically paid a pre-set flat fee for their work, which did not depend on the size of the project itself, and which was passed on to the property owner and financed through the special assessment. This approach effectively freed up resources that the other C-PACE programs used to develop and expand their programs. According to District leadership, it began passing on certain project-specific costs, such as for legal services, to property owners in recent years, but it has not begun passing on costs related to the technical review of projects or project completion certification—nor has it determined the portion of the program administrator's overall compensation that can be directly attributable to this technical work or the specific costs that can reasonably be passed on to property owners.

Third, compensation the District pays to its contracted program administrator, the District's largest operating expense, is structured in way that is both unpredictable and unrelated to the cost of providing core program responsibilities. The fees paid to the program administrator are derived solely from the percentage split of the one-time 83 percent administrative fee assessed for each project approved by the Board. This could result in a high revenue ceiling if the program administrator were to close many large-dollar value projects, or a low revenue floor if the program administrator were to close few small-dollar projects. As is evidenced in Exhibit 5 earlier in this report, the amount paid to the program administrator ranged from $517,000 to $210,000 between 2016 and 2023. This fee bears no relationship to the actual costs of the program administrator to generate a high or low volume of projects. Further, this fee is highly variable and is dependent on the volume of projects the program administrator works on. In some ways this makes sense—the more projects, or the more complicated the project, the more effort is required to process the application and the more funding will be available to the program administrator.

However, processing applications and closing projects represents just one of three core responsibilities for the program administrator, with the others being financial management (administering all special assessments with counties) and marketing and outreach. The expected

level of effort should be both predictable and agreed-upon by the Board or District management, and the resources required to perform these functions should be commensurate with the effort required. Yet the District has not determined what level of resources should reasonably be required to perform these functions, nor has it determined the potential impact that declining program administration fees could have on the program administrator's ability to perform marketing and outreach activities. It is feasible that declining program administration fees could reduce the resources available for marketing and outreach, which could, in turn, lead to fewer C-PACE projects.

While the District has not determined what level of resources should reasonably be required to perform these functions, SRS stated in interviews that the scope of work outlined in its contract with the District requires two full-time equivalent employees with a total baseline cost of approximately $300,000. The District's first contract with SRS included a fixed fee of approximately $310,000 per year for the initial 2 years of the C-PACE Program, which included building the program from the ground up. Beginning in the third year of the contract, the fixed fee expired and the District transitioned to a commission-based fee structure. As described in the background section of this report, SRS was paid a portion, as much as 90 percent, of the program administration fee; while the formula for determining compensation for SRS evolved over the years, it remained a commission-based model. Had the District established a model that identified and funded baseline services required to run the C-PACE program, estimated at $300,000 per year, it would have expended approximately $1.8 million in personnel costs between 2018 and 2023; instead, it paid more than $2.3 million in commission to the program administrator. During this same period, the District received $773,000 in grant funds. Had the District employed a different compensation model, it could have reduced its expenses and, therefore, significantly reduced its reliance on grant funds.

- <u>Programmatic Changes to Generate Additional Revenue</u>—We researched similar programs in 13 other states and found that some have implemented alternative methods to help provide financial sustainability that the District has not explored. Exhibit 8 summarizes information about how eight states, including Colorado, administer and finance operations costs for their energy improvement programs, which could offer potential opportunities for changes in Colorado's C-PACE program.

EXHIBIT 8. COMPARISON OF HOW OTHER STATES ADMINISTER AND FINANCE ENERGY IMPROVEMENT PROGRAMS

State	Program Admin. Fee	Maximum Program Admin. Fee	Annual Collection Fee	Property Owner Pays for Building Performance Review	Maximum assessment repayment term	Entity that Collects Loan Payments
Colorado	2.5%	$75,000	Up to $1,000	X	25 years	Participating counties
Connecticut	Up to 3%	$50,000	None	X	25 years	Energy improvement district
Michigan	Up to 2%	$150,000	0.25% annual fee on the first $10 million assessed	✓	Lesser of useful life of improvement or 30 years	Capital Provider
Minnesota	None	N/A	0.25% annual fee if through private capital providers	✓	20 years	Energy improvement district
Oregon	1%	No maximum	0.25% annual fee	✓	Weighted average useful life of the improvement	Hybrid model: Capital provider and Energy improvement district
Rhode Island	2.5%	$75,000	$300	✓	25 years	Loan Servicing Company
Texas	Up to 1%	No maximum	0.08% annual fee	✓	Weighted average useful life of the improvement	Capital providers
Utah	3%	$90,000	None	Encouraged but not required	30 years	Capital providers

Source: Information obtained during interviews; program's websites; program guides

- Bonds—The District has not issued any special assessment bonds as of December 31, 2023, and has not considered the need to issue them. As noted earlier, statute requires the District to issue bonds "for the purpose of generating the moneys needed to make reimbursement or a direct payment to district members and to pay other costs of the district" [Section 32-20-108(1), C.R.S.]. Colorado Energy Office staff and current Board members reported that they did not have the historical knowledge to explain why the District has not issued any bonds but agreed that this source of potential revenue should be revisited.

Why does this problem matter?

The District's business model has resulted in several potential problematic consequences:

- Because the District has not implemented a sustainable financing approach, the District relies on taxpayer dollars to help pay for its operations since the salaries and benefits of CEO staff are funded with money from Colorado's General Fund. In legislative hearings, proponents of the District and the C-PACE program asserted two critical attributes of the enabling legislation. First, only individuals or businesses that specifically volunteered to participate in the program would incur any costs associated with the program. That is, only those commercial enterprises that are located within counties whose boards adopted a resolution and applied to join the District would incur any costs of the District's creation. Second, no taxpayer monies would be used to fund the District or to fund the capital projects of private commercial enterprises. In addition to direct state support of the District, state and/or federal tax dollars also support the District in the form of grants.

- The District's dependence on grant funding from the Colorado Energy Office could put the District in a vulnerable financial situation. Should the decision be made not to provide the District with grant funding for any sustained period of time, the District's ability to operate with a positive cash flow could be in jeopardy.

- Unless the District changes how it generates revenue to fund its operations, recent trends indicate the District's ability to fulfill its statutory obligation to service special assessments for the full life of the 25-year loans could be in jeopardy. While the number of new projects approved by the District has declined each year since 2019, the number of special assessments the District has to process each year for existing projects continues to increase. As shown in Exhibit 9, between Calendar Years 2019 and 2023, the number of special assessments the District processed increased substantially, from 30 to 94 special assessments. At the same time, the number of projects that have been closed since Calendar Year 2019 has been declining. The District must create better financial stability so it can sustain its operations even if the number of new projects continues to decline.

EXHIBIT 9. PROJECTS CLOSED AND SPECIAL ASSESSMENTS PROCESSED, CALENDAR YEARS 2016-2023

	2016	2017	2018	2019	2020	2021	2022	2023
Projects Closed	3	7	24	26[2]	22	19	15	10
Special Assessments Processed[1]	0	3	7	30	50	66	81	94
Program Administration Fees Collected	$3,000	$167,000	$501,000	$608,000	$559,000	$528,000	$390,000	$255,000

Source: District's C-PACE Program Impact Statement

Notes: [1] The number of special assessments processed per year varies from the cumulative number of projects because some assessments were repaid early or began repayment more than 1 year later.

[2] The "Program Impact Statement" provided by the District indicates 26 distinct projects; however, the "Commons at Inverness" subprojects appear to be listed separately. The count displayed in the table reflects the District's Program Impact Statement.

- The District's ability to issue bonds in a manner favorable to potential applicants necessitates a positive bond rating. Consistent with this, statute requires the District to engage in sound underwriting and business practices to ensure a bond rating necessary for a successful bond sale [Section 32-20-105(4), C.R.S.]. Should the District seek to issue bonds in the future, operating with a negative cash flow and remaining unable to achieve financial sustainability heighten the risk that the District could receive a negative bond rating in the future.

Recommendation No. 1

The Board of Directors for the Colorado New Energy Improvement District (District) should take steps to achieve financial self-sustainability for the District by:

A. Defining the District's management structure and resource needs, particularly related to personnel resources. Consideration should be made to whether the staffing resources will consist of internal employees, full-time or part-time staff, and/or external service providers.

B. Enhancing budgeting and rate-setting practices by developing and implementing a process to routinely analyze (i) projected administrative fee revenue based on actual historical data, realistic projections of how many new projects the District is likely to fund, and additional revenue that could be generated if the District were to assess administrative fees throughout the life of each funded project; and (ii) the true cost of operating the District, including the cost of replacing staffing support provided by the State.

C. Based on the analyses conducted in Parts A and B, considering whether it is necessary to adjust (i) the administrative fee amount the District charges at the beginning of each project and the annual assessment collection fee, (ii) compensation paid to third-party service providers, and (iii) the portion of District costs that can be passed on to property owners.

D. Evaluating whether to issue bonds to provide another source of financing for eligible energy improvement projects, including the methods the District could employ to incorporate bond financing, and to help pay for the District's operating costs.

E. Evaluating benchmarking data on other state's new energy improvement programs to identify opportunities for restructuring Colorado's program and/or generating additional revenue to finance the District's operations cost.

F. Determining the resources required to conduct the level of marketing and outreach, financial management, and other program or administrative activities of the C-PACE Program, and, if necessary, changing the amount of compensation the District pays third-party service providers to perform those activities.

Response

Colorado New Energy Improvement District

A. Agree
Implementation Date: June 30, 2025, and Ongoing

The Board agrees with this recommendation and understands the importance of developing a clear management structure for the District. The Board views management and understanding the necessary staffing requirements of the District as important steps to become financially self-sustaining in line with one of the intended goals of the Colorado C-PACE Program ("Program").

The Board has begun to evaluate the District's full-time, part-time or contractual staffing needs. Following a period to evaluate the final audit report and recommendations, the Board intends to implement elements of the preferred management/staffing plan on or before July 1, 2025. The Board will evaluate the operational needs of the Program including whether to hire internal staff and/or outsource the external staffing needs to sustain and grow the Program and manage the day-to-day operations of the District. This work will include developing a formalized management structure regarding Program operations in order to provide increased accountability to the Board regarding the District's goal of financial self-sustainability.

B. Agree
Implementation Date: June 1, 2027, and Ongoing

The Board agrees that there is an opportunity for an improvement in the process to accurately forecast projected project closings and analyze subsequent revenue projections based on realistic historical project closing data. The Board has implemented process improvements in prior years to use conservative project closing estimates while developing annual budgets and is committed to refining and improving that process.

(i) The Board agrees that it needs to re-evaluate the operational costs of the Program based on the lower project volumes experienced in 2022 and 2023 in order to determine what adjustments may be made to the District's annual servicing fee or if there are additional fees or charges that may be implemented by the District in order to support or offset Program administrative costs. The Board is committed to completing an analysis of the necessary fee structure to best support the Board's goal of ensuring the long-term financial self-sustainability of the Program.

(ii) The projected revenue from assessment and fee closings will be considered by the Board to cover staffing and other operational costs, once the operational costs of running the program, and special district are well understood by the Board.

The Board will evaluate this under recommendation #1 before committing to replacing in-kind staff support from the State. Once the District is generating sufficient revenues from program administration fees, annual servicing fees, and additional revenue streams, the District plans to onboard fulltime or part-time staff or external service providers to best support the ongoing needs of the Program.

The Board foresees an approximate timeline of: June 2025 to finalize its analysis of all Special District operational costs (i). June 2026 to implement a recommended revised fee structure program update through assessment collections (ii). June 2027 as an approximate timeline to begin making meaningful progress, to cover operational costs, through closing fees and revenue from assessments. The Board will begin finalizing its long-term plan to replace State staffing support with District employees and/or external service providers, dependent on the District's availability of funding, and revenue projections.

C. Agree
Implementation Date: July 1, 2025

The Board agrees that the analysis above should be implemented, and the fee structures should be adjusted accordingly.

(i) The District's Board will review the analysis of the administrative fee amounts and the annual assessment collection fee (annual servicing fee) and adjust these accordingly for implementation by the Program by the target implementation date set forth above.

(ii) The Board agrees that the District should solicit market feedback on compensation to third party service providers though a request for information (RFI), request for proposals (RFP), or similar solicitation for open market bids. Upon completion of this solicitation process the Board will develop a plan for better managing the operational costs of the Program and adjust compensation paid to service providers accordingly.

(iii) The Board agrees that based on the needs of the Program, the Board will develop a plan for passing on certain costs of the Program to property owners, including but not limited to costs associated with completing necessary technical reports or eligible improvement verification documents as a condition of closing on Program financing.

D. Agree
Implementation Date: January 1, 2026, and Ongoing

The Board agrees that a bond issuance evaluation should be conducted in the future. However, given the cost and level of resources associated with this type of evaluation, the Board wants to wait to begin this process until the other recommendations have achieved meaningful progress for the District.

The Board recommends pursuing a bond issuance evaluation once the District has become financially self-sustaining, has developed a clear management/staffing plan, and projects sufficient District revenue to cover District operational costs. These steps are important to ensure the District is able to secure an attractive bond rating. Once these initial steps have been completed, the Board is committed to engaging with public finance counsel to understand how a bond issuance may best support the self-sustainability goals of the District.

E. Agree
Implementation Date: June 30, 2025, and Ongoing

The Board agrees that understanding other state's best practices and revenue generating processes (or other opportunities from other leading state's programs) should be initiated and evaluated on an on-going basis. This process will begin at the conclusion of the State's fiscal year and be an ongoing process. Based on ongoing evaluation of selected state programs' "best practices" – the Board anticipates that elements of the same may be applied to or adopted for the Colorado C-PACE

Program, in order to assist the Board with ensuring the long-term financial sustainability of the District.

The implementation date is reflective of the timeline for conducting the evaluation and ultimately beginning the implementation of benchmarking best practices.

F. Agree
Implementation Date: June 30, 2024

The Board agrees with this recommendation and will begin to implement the same, including soliciting feedback from the marketplace on the best allocation of these Program-related costs.

The Board may issue a RFI, RFP or similar solicitation in order to gain additional information related to the costs associated with distinct Program components including marketing and outreach, financial management, and other administrative support activities of the C-PACE Program, in order to assist the Board with determining an appropriate allocation of financial resources to these Program components in the future.

The Board agrees that upon completion of its market research (including but not limited to a RFI, RFP or similar solicitation), the Board may seek to amend or establish the compensation structure for existing or new third-party service providers of the District.

Finding 2 – District Performance

The purpose of the District is to provide an avenue through which public and/or private investment could commit significant and sustainable funding for increased construction of new energy improvements in order to achieve three key objectives:

- To benefit individual commercial property owners by providing a potentially advantageous financing mechanism that would otherwise be unavailable to them,
- To improve ambient air quality and reduce greenhouse emissions by decreasing the use of traditional nonrenewable fuels, and
- To create jobs and stimulate the economy by directly creating jobs for contractors and other persons who complete new energy improvements, and by reinforcing the leadership role of the state in the Colorado energy economy, thereby attracting new energy manufacturing facilities and related jobs to the state.

According to statute, meeting these three objectives would provide "a meaningful, practical opportunity for average citizens to take action that will benefit their personal finances and the economy of the state, promote their own and the nation's energy independence and security, and help sustain the environment" [Section 32-20-102(1)(a)(VI), C.R.S.].

What audit work was performed and what was the purpose?

We reviewed statutory requirements related to the performance of the C-PACE program and interviewed program personnel and Board members. We reviewed performance data generated by the District and the program administrator, analyzed trends, and evaluated the District's performance in achieving its objectives from 2016 through 2023. In addition, we reviewed peer C-PACE programs in 13 other states to identify comparable and alternative practices, including how those practices might contribute to successes. Finally, we reviewed records for a sample of 10 C-PACE projects that were closed between 2019 and 2022 and evaluated them for compliance with statutory requirements and key program parameters. The purpose of the audit work was to determine whether the program is achieving its intended purposes established in statute.

How were the results of the audit work measured?

- **Performance Metrics.** The purpose of the District is to provide an avenue through which public and/or private investment could commit significant and sustainable funding for new energy improvements in order to stimulate the economy by benefiting individual commercial property owners and creating jobs, while improving ambient air quality and reducing greenhouse emissions. Statute requires the District to track key performance metrics intended to measure how well the District is achieving the purposes for which it was created, and to report such information to the state, veterans, and military affairs committees of the General Assembly by March 1 of each year [Section 32-20-105(3)(g), C.R.S.]. This includes the following program metrics:

1. Quality of new energy improvements for which the District has made reimbursement or a direct payment, if deemed necessary by the Board;
2. Total energy savings achieved;
3. Number of program participants;
4. Total amount paid to contractors;
5. Number of jobs created;
6. Number of defaults by program participants and total losses therefrom; and
7. Total amount of bonds the District has issued.

Consistent with this requirement, the District established several key metrics that align with and add to the metrics prescribed in statute to track and evaluate its own performance, including metrics related to operational activity outputs, environmental and economic impacts, and financial metrics. These metrics are outlined in Exhibit 10.

EXHIBIT 10. DISTRICT PERFORMANCE METRICS

Metric Category	Explanation	District Utilized Metrics
Operational Activity Outputs	Serve as direct indicators of the output of the District's efforts.	Volume of applications received, number of projects completed.
Environmental and Economic Impacts Estimates	Quantitatively estimates the economic and environmental impacts of completed projects.	Projected energy savings (kBtu[1]/year) and job-years (i.e., average jobs created per year divided by the number of years) created.
Financial Metrics	Represents common financial indicators.	Operating revenue, operating expenditures, and cash flow.
Efficiency Metrics	Used to determine the relationship between operational activity outputs, or environmental impact estimates, and financial inputs.	Operating expenditures per application processed and operating expenditures per kBtu/year equivalent to the number of cars removed from the road.[2]

Source: Sjoberg Evashenk Consulting-generated based on performance metrics and reporting provided by the District

Notes: [1] BTU stands for British thermal units, which measures heat energy. Each BTU equals the amount of heat needed to raise 1 pound of water 1 degree Fahrenheit. A kBtu equals 1,000 BTU.

[2] The District measures the environmental impact of its energy improvements by determining the amount of energy from non-renewable sources (e.g., fossil fuel-generated power in cars) that would be consumed by existing or traditional infrastructure (e.g., natural gas burning heating units) and the amount of energy from non-renewable sources that would be consumed after the installation of energy-saving infrastructure (e.g., solar power). This is a common way to measure the reduction in the consumption of energy generated through non-renewable sources, which is a primary source of greenhouse gas emissions.

Statute emphasizes the importance of achieving a positive savings-to-investment ratio when establishing special assessments on commercial properties. Specifically, statute defines a special assessment as "a charge levied by the district against eligible real property specially benefited by a new energy improvement for which the district has made or will make reimbursement or a direct payment that is *proportional to the benefit received from the new energy improvement and does not exceed the estimated amount of special benefits received* or the full cost of completing the new

energy improvement" (emphasis added) [Section 32-20-103(14), C.R.S.]. A savings-to-investment ratio greater than one indicates that the project will generate positive cash flow based on utility cost savings. In some cases, a savings-to-investment ratio will fall below 1.0 because energy efficiency projects may be coupled with non-energy efficiency projects. For instance, the installation of solar panels alone may produce a savings-to-investment ratio greater than 1.0, but if a property owner needs a new roof and decides to add solar panels as part of the project, the total cost of the project may result in a savings-to-investment ratio less than 1.0. Therefore, while statute does not specifically state that a savings-to-investment ratio must be equal to or greater than 1.0, it does require that the special assessment "does not exceed the estimated amount of special benefits received *or* the full cost of completing the new energy improvement." A savings-to-investment ratio can be calculated only for projects that involve improvements to existing buildings (not new construction) since the only way to calculate this savings reliably is to know the cost of an existing facility.

- **Program Requirements.** While statute prescribes certain performance metrics to demonstrate the District's success in achieving program objectives, it also prescribes certain guardrails to protect the interest of parties that may be negatively impacted by a potential default: the property owner and the lender(s) whose existing liens were subordinated to the C-PACE lien. The C-PACE Program was adopted in 2013 following a financial crisis that impacted both lenders and property owners. Ensuring that C-PACE loans were prudent and not predatory was a significant matter of discussion during legislative hearings about the enabling legislation for the C-PACE Program. As a result, statute requires the District to adhere to certain parameters when permitting private commercial property owners to utilize public resources. For example, statute [Section 32-20-105(3), C.R.S.] requires the District to verify that projects financed through the program are properly screened before the C-PACE loan is approved. Completed projects are also required to meet certain standards. These requirements are intended to, in part, protect the interests of pre-existing lienholders (such as mortgage holders) and to ensure the long-term success of the project. These requirements include:

    - Credit-Worthiness. Statute requires that the District "establish such standards, guidelines, and procedures, including but not limited to standards of credit-worthiness for qualification of program applicants, as are necessary to ensure the financial stability of the program and otherwise prevent fraud and abuse" [Section 32-20-105(3)(g), C.R.S.]. Further, the District's C-PACE Program Guide, from 2021 forward, consistently required participants to adhere to these credit standards: "The property owner must be current on all real property taxes; have no outstanding involuntary liens, collections, or charge-offs; be current on existing mortgages; and may not be in, or have filed for, bankruptcy in the past 3 years." While the District does not establish the underwriting requirements for C-PACE financing—underwriting is performed at the discretion of third-party capital providers—standards of credit-worthiness were incorporated into legislation as program eligibility criteria during the financial crisis to protect property owners from predatory lending and capital providers from taking on undue risk.

    - Post-Construction Inspection and Certification. Statute requires the District to "take appropriate steps to monitor the quality of new energy improvements…if deemed necessary

by the board" [Section 32-20-105(3)(g), C.R.S.]. Consistent with this, the District's contract with SRS requires the program administrator to (a) conduct on-site inspections to verify project installation and (b) prepare a post-construction commissioning oversight report, when applicable.

Historically, the District required projects to undergo a post-construction evaluation to ensure that the energy improvement project funding generated the benefits described in the application and that ultimately justified the District's approval of the project's participation in the C-PACE Program. Until 2021, the District's Program Guide, which establishes the process for all C-PACE application processing, required the program administrator to prepare and submit this "Commissioning Oversight Report" at the completion of a project. In 2021, the program administrator modified the Program Guide to instead require project owners to prepare and submit a "Completion Certificate" to the capital provider, who must then send a copy of the "Completion Certificate" to and the District upon confirming that a project is complete. Similar to the Commissioning Oversight Report, the purpose of the Completion Certificate is to affirm that the funding provided resulted in the expected improvements and outcomes that were outlined in the project application. Specifically, the 2021 Program Guide states: "while not required, a more formal commissioning effort, conducted by a third party, is recommended for projects with greater complexity, uncertainty, or savings at risk. Moreover, upon construction completion, the property owner shall issue to the capital provider one or more certificates of completion… A copy of each fully executed Completion Certificate will subsequently be provided by the Capital Provider to the District."

What problems did the audit work identify and why does it matter?

Overall, we found that the District has reported all required information to the General Assembly, as directed by statute. Specifically, each year the District's annual reports generally include metrics as required by statute.

While the District reports this information annually, it does not provide an analysis of these metrics, such as trends over time, or a discussion of overall program performance. Our analysis of the data and other information that the District reported indicates that the District may be becoming less effective and less efficient at achieving its performance goals. Specifically, the District's performance measures show that the C-PACE program is producing fewer results—fewer projects, fewer interested applicants, fewer jobs created, and less energy savings and greenhouse gas reductions—than it produced 5 years ago. At the same time, the cost to produce these results has increased. As a result, the C-PACE Program may not be fulfilling its purpose to benefit individual commercial property owners, improve the environment, and stimulate the economy.

Performance Metrics Reported to General Assembly in March 2022	
Projects Closed:	19 projects
Amount Financed:	$64,179,852.98
Projected Energy Savings:	23,415,199 kBtu/yr
Projected Lifetime Cost Savings:	$13,897,768
Counties Opted Into District:	39 counties
Qualified Capital Providers:	45 capital providers
Jobs Created:	676 job-years
Registered Contractors:	231 Energy Efficiency 160 Renewable Energy 16 Water Conservation
Bonds Issued:	$0.00
Amount Paid to Contractors:	$0.00

At the same time, we found that the District complied with some program requirements, including those relating to the application, eligibility verification, project review and approval, and other key program requirements. However, our analysis of project files revealed that the District did not always adhere to other program requirements designed to protect consumers against predatory lending and capital providers against undue risk of default.

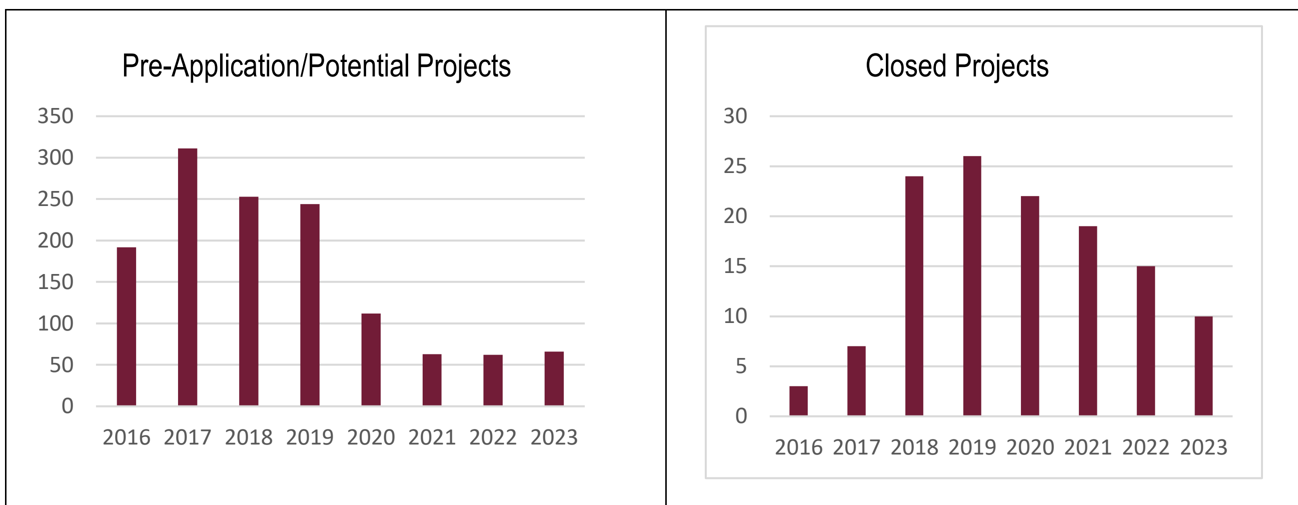
We address both issues below.

Performance Metrics Suggest Declining Effectiveness and Efficiency

We reviewed the performance metrics prepared by the program administrator and the District and found the following:

- **Program Participation**. Project data show that the District has been receiving fewer applications from commercial property owners each year since 2018. Similarly, the number of closed projects has declined each year since 2019. This is illustrated in Exhibit 11. The economic and environmental impacts of the District are determined by the volume of projects financed through the C-PACE program, as is the financial sustainability of the District. Declining projects indicates diminished outcomes, for which the District was created, and diminished capacity of the District to support its own operations.

EXHIBIT 11: PROPOSED AND CLOSED NEW ENERGY IMPROVEMENT PROJECTS 2016-2023



Source: Annual C-PACE Program Impact Statements, District Annual Reports to the Colorado General Assembly, and the program administrator's performance metric tracking spreadsheets

In addition to requiring the program administrator to process and close project applications, the District's contract with SRS requires the program administrator to perform a variety of additional functions, including enrolling capital providers, capital improvement contractors, and counties into the program, as well as conducting general program marketing and outreach (e.g., informational workshops). These activities are intended to increase the footprint of the C-PACE Program in the State. Performance metrics produced by the program administrator show a general reduction in outputs in each of these areas in recent years when compared to the early years of the formation of

the C-PACE Program. Exhibit 12 illustrates declining or stagnating trends for each of these metrics. Although the aggregate number of capital providers, contractors, and counties enrolled in the C-PACE Program continues to increase—despite the declining number of newly enrolled parties—this is not translating to increased project applications or closed projects.

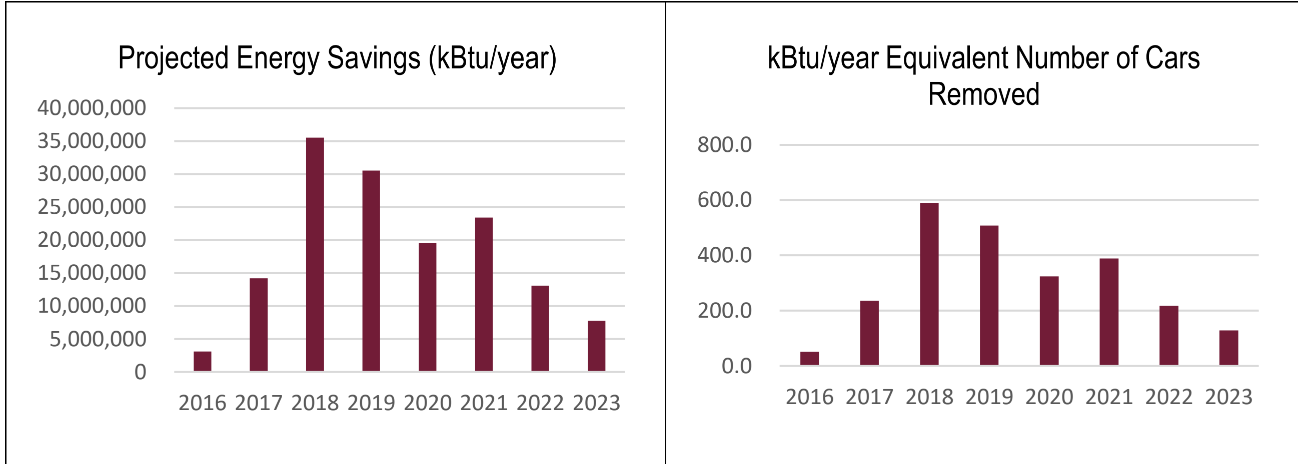
EXHIBIT 12: ADDITIONAL METRICS RELATED TO THE PROGRAM ADMINISTRATOR'S PRIMARY RESPONSIBILITIES

Source: District performance metric data provided by the program administrator

It is reasonable to assume that the number of capital providers, contractors, and counties enrolled in the C-PACE Program would diminish or become stagnant over time, as there is a finite number of each. However, the District's contract with the program administrator with a commission- or fee-for-service payment provision suggests that the District has expected continued service levels—and outputs—over the course of its contractual relationship with SRS since 2015.

- **Environmental Impacts.** Performance statistics show declining environmental impacts of the C-PACE Program since 2018. Specifically, the projected energy savings from projects decreased from 35.5 million kBtu savings in 2018 to 7.8 million ktBu savings in 2023—a substantial decline of 78 percent. Similarly, the energy savings equivalent to the number of cars removed from the road has decreased from 590 in 2018 to about 129 in 2023—a 78 percent decline over 5 years. This means that, while the District continues to have a positive impact on the environment, its overall environmental impact has been in decline. This is illustrated in Exhibit 13.

EXHIBIT 13: ESTIMATED ENVIRONMENTAL IMPACT, CALENDAR YEARS 2016-2023

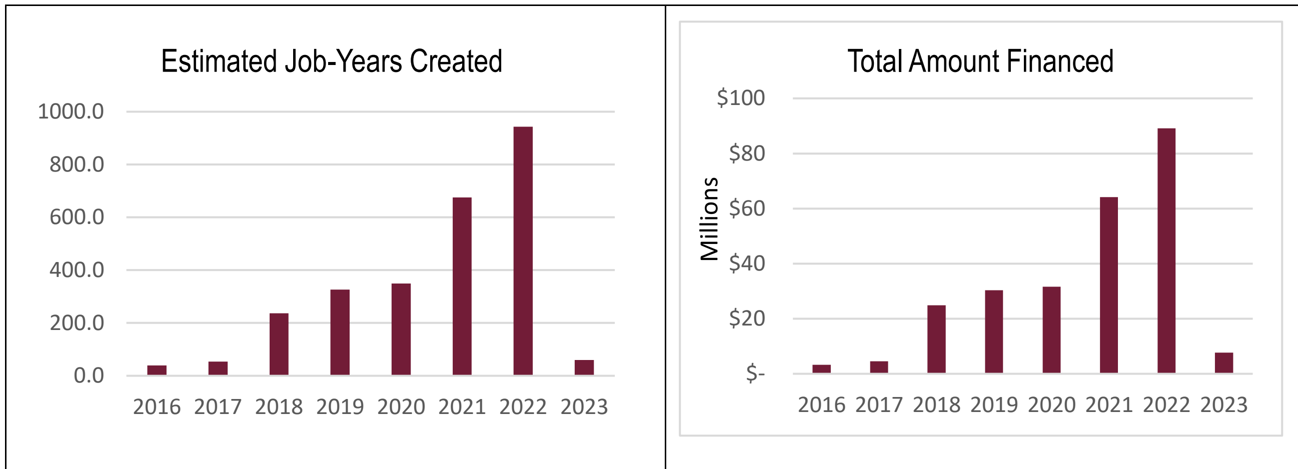


Source: Annual C-PACE Program Impact Statements

- **Economic Impacts.** We reviewed data related to two economic impact indicators.
    - **Job years.** Energy efficiency projects contribute to job creation. A "job year" is a metric that represents the resources required to employ one full-time equivalent employee for 1 year and indicates the job creation impact of a specific project.[1] The number of job years created by the C-PACE Program increased between 2018 and 2022, which indicates a positive economic impact. However, the number of job years decreased significantly in 2023. This indicates that despite declining project volume, the C-PACE Program continued to achieve positive economic impacts. This is primarily because Job-Years created is related to both the volume of projects and the size of the projects. An indicator of the size of the projects is the total amount financed. In 2021 and 2022, the District experienced a significant increase in the dollar amount financed despite declining program participation. However, in 2023, the number of job-years created fell to its lowest point since 2017 because both the number of projects completed and the amount financed in 2023 were at their lowest points since 2017. These trends are illustrated in Exhibit 14.

[1] According to SRS, it calculates job years using standards established by the American Council for an Energy-Efficient Economy.

EXHIBIT 14: ECONOMIC INDICATORS, CALENDAR YEARS 2016-2023



Source: Annual C-PACE Program Impact Statements

- **Contractors Performing Work.** The District did not report all monies paid to contractors, as required by statute. Between 2016 and 2023, the District reported that it spent $0 on contractors performing work on energy improvements since the District does not pay those contractors directly; rather, the District pays capital providers, who remit monies to property owners, who then pay the contractors. Specifically, annually, the District reports $0 as the "total amount paid to contractors *for improvements*" (emphasis added). However, statute requires the District to report the total amount paid to *all* contractors. As noted previously, the District hires third-party professional service firms for District operations, including the program administrator, accounting and auditing service, legal services, and other technical expertise—some of which is directly related to projects approved by the District. Financial records show that the District paid professional services contractors between $424,000 and $785,200 annually during the period. This is illustrated in Exhibit 15.

EXHIBIT 15. CONTRACT EXPENDITURES, CALENDAR YEARS 2016-2023

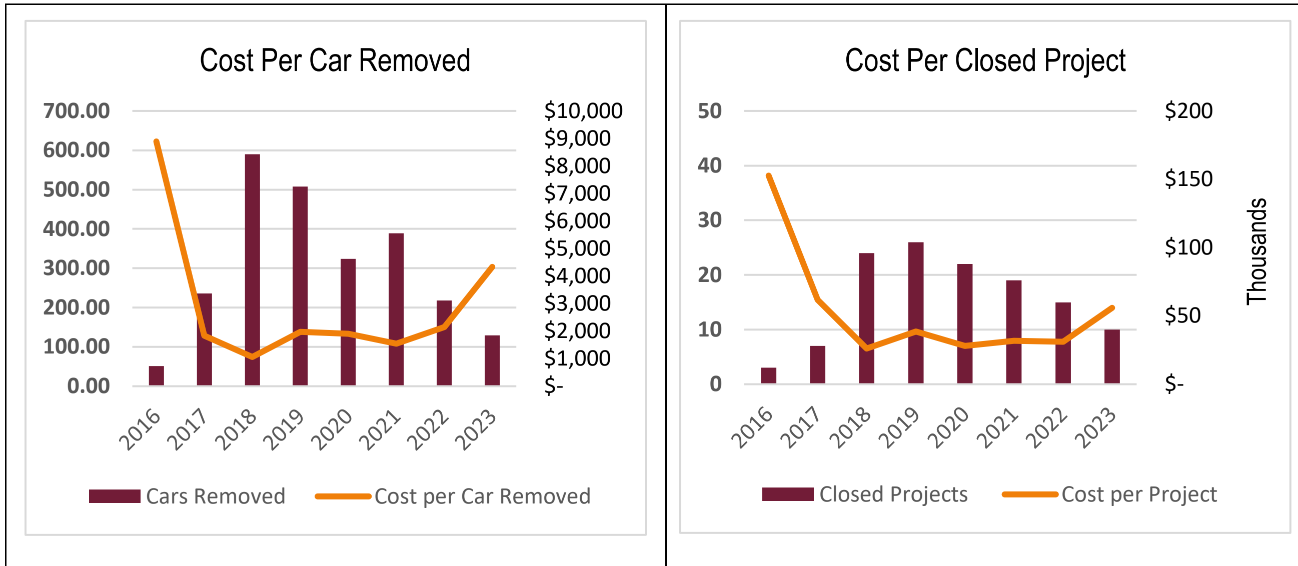
Contract Services	2016	2017	2018	2019	2020	2021	2022	2023
Legal	$24,303	$23,149	$122,327	$134,666	$117,850	$106,096	$95,433	$140,244
Program Administrator Fees	$392,063	$397,880	$450,840	$516,618	$440,955	$428,374	$310,045	$209,957
Facilitator	$18,135	$3,023	$8,678	$9,262				
Audits			$13,043	$99,678	$10,000	$5,550	$5,600	$122,517
Financial Management				$24,982	$33,083	$30,044	$34,085	$45,000
Total	$434,501	$424,052	$594,887	$785,206	$601,888	$570,064	$445,163	$517,718

Source: District financial records, audited financial statements

- **Efficiency Metrics**. The District's cost-per-closed project has steadily increased from $26,000 in 2018 to $44,000 in 2022, an increase of 69 percent, and the cost per car removed equivalent has increased from $100 to $3,000 during the same period. This is illustrated in Exhibit 16. This means that while the C-PACE program continues to benefit property owners, the environment, and the economy, the program's benefits have not only been diminishing since 2018, but the District has

become less efficient at producing the outcomes it was created to produce: property-owner cost savings, greenhouse gas emission reductions, and jobs.

EXHIBIT 16: EFFICIENCY METRICS, CALENDAR YEARS 2016-2023



Source: Sjoberg Evashenk Consulting generated based on C-PACE Program Impact Statement

Compliance with Program Parameters Designed to Protect Investors in C-PACE Projects

While statute prescribes certain performance metrics to demonstrate the District's success in achieving program objectives, it also prescribes certain guardrails to protect the interest of parties that may be negatively impacted by a potential default: the property owner and the lender(s) whose existing liens were subordinated to the C-PACE lien. The C-PACE Program was adopted in 2013 following a financial crisis that impacted both lenders and property owners. Ensuring C-PACE loans were prudent and not predatory was a significant matter of discussion during legislative hearing involving the C-PACE Program. Some projects approved by the District did not adhere to the requirements set forth in statute to protect property owners and lenders.

- **Savings-to-Investment Ratio.** Projects appear to have lower than recommended savings-to-investment ratios. Of the 10 sampled projects, six involved improvements to existing buildings—as discussed above, this ratio can only be calculated for projects involving improvements to existing buildings. Of those six, one project had a savings-to-investment ratio greater than 1.0, at 2.18, indicating that the project will generate positive cash flow based on utility cost savings. However, the other five projects had savings-to-investment ratios less than 1, with one project having a ratio as low as 0.08, and therefore, would not generate positive cash flow based on utility cost savings. This is illustrated in Exhibit 17.

EXHIBIT 17. SAVINGS-TO-INVESTMENT RATIOS OF RECENT COMPLETED C-PACE PROJECTS

Project	Savings-to-Investment Ratio
Project 1	0.29
Project 2	0.08
Project 3	0.12
Project 4	0.67
Project 5	0.47
Project 6	2.18

Source: District Program Impact Statements

Statute does not prohibit improvements that cost more than the savings that will be generated, but a positive ratio is an indicator that the value of the improvement outweighs the payments the property owner must pay over the course of as many as 25 years. Costs that significantly outweigh benefits could impact the value of the property in the years ahead, increase risk for capital providers and other lenders whose liens were subordinated to the C-PACE lien, and also detract from the quality of new energy improvements for which the District has made reimbursement or a direct payment.

- **End-of-Project Reports.** Of the 10 projects sampled, the District reported that four were still under construction as of December 31, 2023; for two of the remaining six projects, the program administrator could not demonstrate that onsite inspections occurred or that either a Commissioning Report or Completion Certificate were submitted to the District, as required. According to the program administrator, the capital providers for these two projects are no longer participating in the C-PACE program and, despite periodic requests for Completion Certificates, have not responded with required documentation. The program administrator noted that it is continuing to reach out to the capital providers, but has not exercised other options—to conduct an on-site inspection or obtain a Commissioning Oversight Report—to ensure the project financed through the C-PACE program adhered to program requirements. The lack of oversight or other confirmation that projects are completed as intended increases risk that projects utilizing C-PACE funding may not produce the promised improvements or yield benefits for which the C-PACE Program was intended.

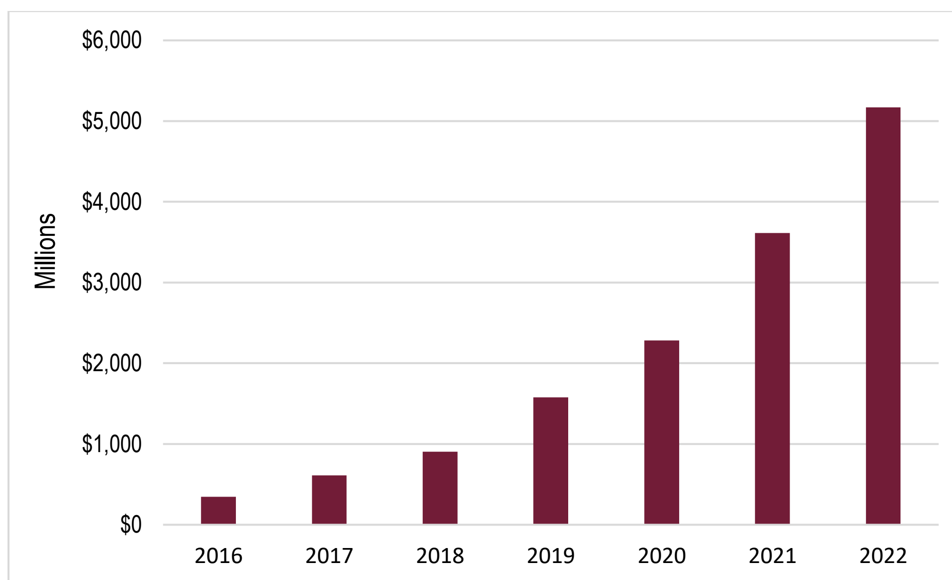
- **Credit Standards.** For all of the 10 projects sampled the program administrator conducted preliminary research to assess the applicant's credit-worthiness via property information available on county assessors' websites, but did not conduct further confirmation of the applicant's adherence to the District's credit standards, such as verifying whether the property owner had filed for bankruptcy in the past 3 years. Due diligence on the part of the program administrator is necessary to mitigate undue risk to capital providers, subordinate lienholders, and the C-PACE Program in general.

The District reported no defaults and that no bonds were issued since the inception of the C-PACE program.

Why did the problem occur?

While some factors outside of the District's control have impacted its performance since 2018, including the COVID-19 pandemic and historically low interest rates available from private lenders, we did not find that these factors alone can explain the stagnating or declining performance the C-PACE Program experienced in the last few years. Of the peer agencies in other states we reviewed as part of this audit, some experienced stagnating or declining performance, while others continued to experience growth. In contrast to the performance of the C-PACE Program, however, the overall trend among C-PACE programs nationwide shows an increasing market for C-PACE financing. According to PACENation, a PACE advocacy nonprofit organization to which the District is a member, C-PACE programs throughout the nation experienced growth in investments every year between 2016 through 2022, as shown in Exhibit 18.

EXHIBIT 18. NATIONWIDE TRENDS IN C-PACE INVESTMENT, 2009-2022



Source: PACENation, a PACE advocacy nonprofit organization

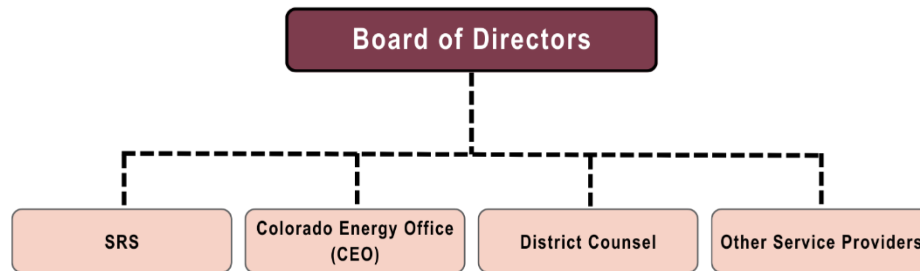
Given these trends, we evaluated the organizational structures, funding sources, and program design of peer C-PACE programs in 13 other states, as well as the impacts of these factors on the performance of their respective programs. In doing so, we identified three factors that may be contributing to the problems that we identified with Colorado's C-PACE Program.

- **Management Structure.** First, while each C-PACE program we reviewed was structured differently—e.g., they were structured as independent non-profits, programs within already-existing state agencies, or housed within independent quasi-state enterprises, such as a state infrastructure bank—the internal organizational structure of each program was generally consistent among different states. Each program had an executive director or program head that was responsible and accountable for the program's success.

  The District, on the other hand, does not have a formalized management structure, nor does it have a chief executive. As noted previously, the District has no employees. Instead, it contracts with a variety of entities, including the CEO, the program administrator (SRS), and a variety of other private

firms, including law firms, accounting firms, and others to provide routine and ad hoc services to the District and help coordinate various other services for and on behalf of the District. None of these entities, nor their employees, serve in the capacity of a chief executive of the District. The District's organizational structure is presented in Exhibit 19.

EXHIBIT 19. COLORADO NEW ENERGY IMPROVEMENT DISTRICT ORGANIZATION CHART



Source: District bylaws and contracts between the District, the CEO, and other third-party service providers

Management is typically responsible for all activities of an organization, including making decisions regarding the acquisition, deployment, and control of human, financial, and other resources, as well as for the design, implementation, and effectiveness of critical programs. While the CEO has provided resources to, and leadership on behalf of, the District, staff of the CEO are not responsible or accountable to the Board of Directors, nor do they have the resources themselves to fulfill the role of executive management of the District. While the CEO is responsible for monitoring the program administrator and carrying out much of the administrative and ministerial functions of the District, staff assigned to perform activities on the District's behalf also have full-time responsibilities with the CEO, and according to staff, have limited resources to monitor and oversee all of the work of the program administrator. The lack of formalized management and oversight makes it challenging to both realize the program's overarching goals and develop a strategic plan to achieve said goals. Without a clearly defined management structure, including a designated chief executive who is both responsible for the District's operations and accountable to the Board of Directors, the District may not be able to optimize its performance and ensure compliance with all program requirements.

- **Reliance On Third-Party Program Administrator.** Second, each peer agency used the "program administrator" in a manner that was different than the District. Rather than assigning the bulk of the programs' operational responsibilities to a third-party program administrator, each of the other states employed a firm to perform a narrow set of responsibilities related to the technical review of projects, both during the pre-approval and eligibility review process and, sometimes, in the post-construction verification process. As noted previously, this technical reviewer was typically paid a pre-set flat fee for their work, which did not depend on the size of the project itself.

  Conversely, the District allocates up to 83 percent of its fee revenue to the program administrator, which is responsible for vetting all projects, just as technical reviewers do on behalf of peer agencies in other states, but is also responsible for marketing and performing certain financial management functions of the District, as described earlier. The District's contract with the program administrator does not require that the program administrator allocate any particular portion of fee revenues to

these distinct activities. Because of this, unlike other peer agencies, the Board is unable to determine how the vast majority of District resources are allocated to various District activities, including marketing and outreach. Board members we interviewed expressed a concern that the current model does not give the Board enough control over the District's limited resources, and that marketing and outreach was suffering as a result. Employing an alternative model, one similar to the peer agencies reviewed as part of this audit, could potentially result in the District having additional resources to help manage its operations, and give the Board greater control over how District resources are allocated.

- **Loan Origination.** Third, some C-PACE programs that are able to originate their own loans tend to have been more successful than those that rely solely on third-party capital providers. Two of the peer agencies reviewed, Connecticut and Minnesota, offer financing directly through their C-PACE program, in addition to third-party financing. Originating C-PACE loans directly allows these programs to keep the revenue from repayments, which can then be re-invested. As a result, these programs report that they are not merely sustainable, but profitable. In addition, by originating their own loans, these other programs have the ability to offer lower interest rates than third party capital providers. Offering lower interest rates makes the program more attractive to property owners, which results in a higher volume of projects closed. As shown in Exhibit 20, Minnesota and Connecticut had the highest project volume in 2016 to 2022, among five of the other states' programs that provided relevant data for review as part of this audit.

EXHIBIT 20. PEER C-PACE AGENCIES BY PROJECTS CLOSED, 2016-2022

Program	Projects Closed, 2016-2022
Minnesota	403
Connecticut	266
Colorado	116
Texas	71
Michigan	64
Rhode Island	33[1]

Source: Program documentation provided by administrators of C-PACE programs within each state

Note: [1] Rhode Island gave only a cumulative total of projects closed, so this figure may include projects in 2015 and 2023.

Minnesota and Connecticut both received public funding for the initial "seed money" to begin to originate loans. The District was also provided with seed funding from the CEO, just over $1.2 million in grant monies, but that funding was earmarked for the development of a loss reserve which was statutorily required to ensure a positive bond rating. As discussed in the first finding, the District has not issued any bonds although they could provide a mechanism for the District to reduce its reliance on third-party capital providers to finance projects that are approved for participation in the C-PACE Program.

Addressing these factors will require rethinking the structure of the District, the role of the program administrator, and the contract under which the program administrator operates. The Board appears well positioned for this reassessment. Members raised these concerns during this audit, and in open meetings; it also took action to extend the current contract with the program administrator until June 30, 2024, midway through its fiscal year, with the intent to consider the findings of this audit before determining its next steps.

Recommendation No. 2

The Board of Directors (Board) for the Colorado New Energy Improvement District (District) should evaluate alternative governing structures for the District to improve overall District and program performance, which should include:

A. Considering whether it would be feasible to establish a formal management structure with an appointed chief executive who is responsible for Board operations and accountable to the Board. This could involve hiring District employees or contracting with third parties, but should result in clearly defined management roles and responsibilities.

B. Considering options to restructure the District's contract with the program administrator to ensure that the Board retains discretion regarding how District resources are allocated, and the District retains the ability to charge property owners all fees necessary for closing loan applications.

C. Evaluating the cost-benefit of issuing bonds in order to originate loans through the District.

Response

Colorado New Energy Improvement District

A. Agree
Implementation Date: June 30, 2025

The Board agrees with this recommendation and will need to understand best practices from other programs, the true operational costs of running the Program and undertake further analysis to determine the best structure for Program management and executive Program oversight.

The Board is committed to developing a management/staffing plan for the District and is further committed to ensuring that the plan has a high level of Board support prior to implementation, including analyzing whether the management/staffing plan is best undertaken by full-time or part-time District employees, third-party service providers, or a hybrid model.

B. Agree
Implementation Date: June 30, 2025

The Board agrees with this recommendation and will consider all options to restructure the contract with the current program administrator to ensure the District retains discretion to determine: (1) how District resources are most efficiently allocated, and (2) the amount of fees and charges to be collected from property owners/District members to best support the long-term financial self-sustainability of the District.

C. Agree
Implementation Date: June 30, 2027

Reference response to Recommendation 1.D. above. The Board agrees that a cost benefit analysis of issuing bonds is important. The Board will begin to analyze this concept and potentially evaluate a bond issuance (to generate funds that may be utilized to originate loans through the District) after the District has made substantial and measurable progress on implementing the recommendations set forth in this performance audit, which will assist the District with securing a favorable bond rating.

The Board would like to ensure that the operational budget could support the cost of this evaluation, before undertaking this process. The implementation date reflects the desire from the Board to accomplish a financially self-sustaining District and operating model before undertaking a bond issuance evaluation.

Following the completion of the bond evaluation at an appropriate future date, the Board will determine whether to pursue a bond issuance or continue with the current Program format with qualified capital providers providing financing for the property owners participating in the Colorado C-PACE Program.