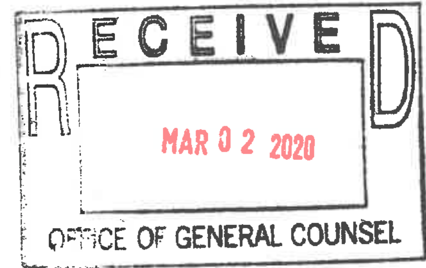
MOUNTAIN WEST FINANCIAL
Making Homeownership A Reality Since 1990

February 21, 2020



Federal Housing Finance Agency
400 Seventh Street SW
Eighth Floor
Washington, DC 20219
ATTENTION: PACE Request for Input, Notice No. 2020-N-1

Regarding: Continuation of PACE Energy Program

To whom it may concern,

This letter is on behalf of Mountain West Financial, Inc., a community lender representing the mortgage industry with its corporate office located in Redlands, California. In addition to Los Angeles and Orange County, Mountain West Financial has a large footprint in the Inland Empire, which comprises Riverside and San Bernardino Counties with San Bernardino County being the largest county in the United States. These two counties combined have a diverse demographic mix, and are equal in size to eight eastern states.

Many homeowners in the area rely on affordable housing, and they are being adversely affected by the Federal Housing Finance Agency (FHFA) and the Department of Housing and Urban Development (HUD) discontinuation of the PACE loan program.

Nationally it is known as PACE (Property Assessed Clean Energy) financing. HERO is a regional term for this loan program. HERO stands for Home Energy Renovation Opportunity. This program provides financing for energy improvements made to homes, e.g. solar, windows, plumbing, etc. where the HERO/PACE firm collects their principal, interest, fees and costs through increased property taxes. Financing of 100% of the improvement costs is available.

As a conscientious lender, one who through prudence and 'doing the right thing' was able to help consumers through the housing crisis of 2008, we care deeply for our borrowers and the communities we serve. However, the discontinuation of the PACE program goes against our mission of "making homeownership a reality" and is a direct contradiction to FHFA's own mission to "ensure that the housing government sponsored enterprises operate in a safe and sound manner so that they serve as a reliable source of liquidity and funding for housing finance and community investment."

Moreover, alternative energy companies and advocates don't agree with this decision. An industry trade group called PACENation feels the decision is not based on evidence and lacks justification. An independent study published by the Journal of Structured Finance in 2016

concluded that PACE projects on average, "are able to recover at least their full costs at resale, whereas most other home improvers are only able to recover about 60%." In general, PACE projects recovered at least 100% of their full costs, usually more.

It is disheartening that the FHFA has taken the stance for Fannie Mae and Freddie Mac to discontinue accepting loans with this feature. However, the PACE marketplace projects this action to be symbolic, rather than tangibly disruptive to the industry. As for concerns about consumer protections, laws have been enacted in California, which we know is the program's largest residential market, to protect PACE participants. By law, PACE transactions have an underwriting standard that's based on income and ability-to-pay. In addition, underwriters at Mountain West Financial, Inc. pull tax rolls and compare them to the preliminary title policy on EVERY loan transaction to ensure that the PACE obligation is accurately reflected in qualifying the borrower.

FHFA has asked for public input on several questions, we wish to respond to at this time:

Question 1
"Should FHFA direct the Enterprises to decrease loan-to-value ratios for all new loan purchases in states or in communities where PACE loans are available?" Our response is no. FHFA's issue is that the lien travels with the property and that FHFA will receive less proceeds than a property that does not have improvement or an assessment. This argument is flawed in the assumption that the property will not appreciate enough in value to offset the lien. In fact, data is submitted herewith regarding an empirical study completed by Goodman and Zhu 2016 (Exhibit C) showing that the "energy efficient improvements increase the value of the property by more than the PACE assessment." A valuation tool was also created for assessing PACE properties.

Question 4
"Should FHFA establish safety and soundness standards for the Federal Home Loan Banks to accept as eligible advance collateral mortgage loans in communities where PACE loans are available?" We welcome viable standards that contribute to the safety and soundness of the Federal Home Loan Banks as well mortgage Enterprises. As a mortgage banker we have the same tenants to adhere to:

- Capital adequacy – money/income to cover business costs
- Asset quality – lending on assets likely to be repaid
- Management – sound decisions
- Earnings – making a reasonable profit
- Liquidity – enough money on hand and in reserves
- Sensitivity – to market risk

A possibility to consider in making sound decisions on PACE loans may be to lower or cap the debt-to-income ratio.

Question 5
"How might the Enterprises best gather or receive information on their existing guaranteed or owned mortgage loan portfolio to understand which loans have PACE liens and in what amount? Should mortgage loan servicers be required to gather and report such information to the Enterprise on a period basis?" Mortgage loan servicers would report information on PACE loans on an annual basis.

Question 6
"Would it be most beneficial for states that authorize PACE programs to require a registry of PACE lending so that information currently only held by PACE vendors or local tax rolls could be available and maintained on an ongoing basis?" Yes, this would be most beneficial. A PACE portal that could be searched by property address, assessor's parcel number, amount of the PACE lien, etc. would be most valuable.

Question 7
"Should servicers ... provide an annual or more frequent notice to existing borrowers. . .that, under the terms of their mortgage PACE liens are not permitted? . . .Should borrowers. . . execute additional agreements or certification. . . guaranteeing the borrowers will not accept PACE financing for energy efficiency improvements?" The California Association of Realtors successfully sponsored AB 2693 (Dababneh), which requires Truth in Lending Integrated Disclosure – or TRID-like disclosures – be provided to a property owner participating in a PACE program, a three-day right of rescission, and a notice that the property owner may not be able to refinance or sell without paying off the PACE "loan." This bill was signed into law by former Governor Jerry Brown. We propose a uniformed nationwide disclosure elaborating what California currently has in effect. We would not support additional restrictions limiting borrowers' rights.

Question 9
"...should loan products issued or guaranteed by the government, such as Federal Housing Administration mortgage insurance, consider adjustments such as risk based mortgage insurance premiums or limits on partial assignment claims...?" The Federal Housing Administration (FHA) appears to be in lockstep with whatever FHFA proposes despite the fact that on July 19, 2016 they published HUD mortgagee letter 2016-11 stating "FHA supports the goals of clean energy, energy efficiency, and resilience. Property Assessed Clean Energy (PACE) programs may provide an alternative means of financing energy and other PACE-allowed improvements to residential properties using financing provided by private enterprises in conjunction with state and local governments." (Exhibit A)

Mountain West Financial
Making Homeownership A Reality Since 1990

Less than seventeen months later "FHA is concerned about the potential for increased losses to the Mutual Mortgage Insurance Fund". (Exhibit B) In the case of FHA loans, these transactions have upfront and monthly mortgage insurance to help mitigate losses. Additionally, these same facts were present in 2016 when HUD accepted this program. There may be a need to increase the percentage of upfront or annual MIP being collected specifically for the PACE product although documented proof supporting this has not been provided. The group PACENation said, the FHA insurance fund has never been adversely affected by these PACE liens. "It is well documented that PACE is a successful tool for helping homeowners make energy efficiency, renewable energy and water conservation improvements that save money and make their homes safer and more comfortable to live in." There is a direct benefit to the homeowner of having an energy efficient home. This is documented by an energy savings report. The decisions made by FHFA and FHA do not deter the fact that people are looking for clean energy options.

Our biggest concerns are not just the possible discontinuation of the programs but also new rules that will complicate the sale of a home that already have a PACE lien preventing the buyer from obtaining financing. It is very disappointing that FHFA and HUD have made a determination that will eliminate one of the principal benefits of PACE, which is transferability of the PACE assessment upon resale, for homes that have this type of financing.

Mountain West Financial, Inc. believes that it's important for consumers to have access to choices, and FHFA's decision to hinder consumer choice in a free market does not best serve our communities. We want to make sure homeowners have access to safe choices, to make homeownership a reality to qualified individuals and families. With the PACE financing option homeowners can make the clean energy upgrades that they want, and in many cases, need to make.

Respectfully,

Carla L. Ferguson
Executive Vice President

Cc: Gary Martell, Jr., President
Michael Delehanty, Chief Financial Officer
Stacy Mohr, Executive Vice President

Attachments:
A – HUD Mortgagee Letter 2016-11
B – HUD Mortgagee Letter 2017-18
C – The Journal of Structured Finance/Urban Institute – July 2016

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

July 19, 2016

Mortgagee Letter 2016-11

To	All FHA Approved Mortgagees All Direct Endorsement Underwriters All FHA Roster Appraisers All FHA Roster Inspectors All FHA Approved 203(k) Consultants All HUD Approved Housing Counselors All HUD Approved Nonprofit Organizations All Governmental Entity Participants All Real Estate Brokers All Closing Agents
Subject	Property Assessed Clean Energy (PACE)
Purpose	This transmits updates to the following sections of HUD Handbook 4000.1, *Single Family Policy Handbook*: • Section II.A.1.a.i(E)(1)(a)(iii), Sales Contract and Supporting Documentation • Section II.A.1.a.iii(B)(6)(e), Additional Requirements When Ordering an Appraisal • Section II.A.1.b.iv(A)(6), Property Assessed Clean Energy (PACE) • Section II.A.4.a.iii(A)(1), Automated Underwriting System Data Entry Requirements • Section II.A.4.d.iii(G)(2), Interested Party Contributions (TOTAL) • Section II.A.5.c.iii(G)(2), Interested Party Contributions (Manual) • Section II.A.5.d.vii(B), Calculating Total Mortgage Payment • Section II.A.6.a.viii(A), Monthly Escrow Obligation • Section IID.12.d.iv, Property Assessed Clean Energy (PACE)

Effective Date

These Handbook sections are effective for all case numbers assigned on or after 60 days from publication of this Mortgagee Letter; however, Mortgagees may begin using the policy immediately.

4000.1 FHA Single Family Housing Policy Handbook

The attached updates to HUD's Single Family Housing Policy Handbook 4000.1 will be incorporated in a future publication of the Handbook.

Background

FHA supports the goals of clean energy, energy efficiency, and resilience. Property Assessed Clean Energy (PACE) programs may provide an alternative means of financing energy and other PACE-allowed improvements to residential properties using financing provided by private enterprises in conjunction with state and local governments.

The terms and conditions of the PACE obligation may vary by state, local government, and PACE program. PACE programs also determine the scope of allowable improvements made under their respective PACE programs. Generally, the repayment of the PACE obligation is collected in the same manner as a special assessment is collected by the local government, rather than paid directly by the Borrower to the party providing the PACE financing. Generally, the PACE obligation is also secured in the same manner as a special assessment against the property. In the event of the sale, including a foreclosure sale, of the property with outstanding PACE financing, the obligation will continue with the property causing the new homeowner to be responsible for the payments on the outstanding PACE amount. In cases of foreclosure, priority collection of delinquent payments for the PACE assessment may be waived or relinquished.

The Department of Energy is updating its Best Practices Guidelines for Residential PACE Financing, which may be used by states and counties to align with their consumer protection goals.

FHA regulations at 24 CFR §203.32(a) require, in part, that with certain exceptions, at the time the mortgage is offered for insurance, the property must be free and clear of any liens other than the FHA-insured mortgage. In addition, FHA regulations at 24 CFR §203.41(c)(2) require that any restrictions on conveyance automatically terminate if title to the mortgaged property is transferred by foreclosure or deed-in-lieu of foreclosure, or if the FHA-insured mortgage is assigned to the Secretary.

Continued on next page

Attached to this ML are additions and revisions to the Handbook 4000.1. The following is a summary of Title II Forward Mortgage policy changes, which is provided for informational purposes only.

Outstanding PACE Obligations

Properties which will remain encumbered with a PACE obligation may be eligible for FHA-insured mortgage financing, provided that the mortgagee determines that the following requirements have been met:

- under the laws of the state where the property is located, the PACE obligation is collected and secured by the creditor in the same manner as a special assessment against the property;
- the property may only become subject to an enforceable claim (i.e., a lien) that is superior to the FHA-insured mortgage for delinquent regularly scheduled PACE special assessment payments. The property shall not be subject to an enforceable claim (i.e., lien) superior to the FHA-insured mortgage for the full outstanding PACE obligation at any time (i.e., through acceleration of the full obligation.) However, a notice of lien for the full PACE obligation may be recorded in the land records;
- there are no terms or conditions that limit the transfer of the property to a new homeowner. Legal restrictions on conveyance arising from a PACE obligation that could require the consent of a third party before the owner can convey the real property are prohibited, unless such provisions may be terminated at the option of, and with no cost to, the homeowner;
- the existence of a PACE obligation on a property is readily apparent to mortgagees, appraisers, borrowers and other parties to an FHA-insured mortgage transaction in the public records and must show the obligation amount, the expiration date and cause of the expiration of the assessment, and in no case may default accelerate the expiration date; and
- in the event of the sale, including a foreclosure sale, of the property with outstanding PACE financing, the obligation will continue with the property causing the new homeowner to be responsible for the payments on the outstanding PACE amount.

Disclosure of PACE Obligation, Terms and Conditions upon Sale

For properties with existing PACE obligations, the property sales contract must indicate whether the obligation will remain with the property or be satisfied by the seller at, or prior to closing. Where the obligation will

Continued on next page

(continued)

remain, all terms and conditions of the PACE obligation must be fully disclosed to the borrower and made part of the sales contract between the seller and the borrower.

Appraisal Requirements

Where energy and other PACE-allowed improvements have been made to the property through a PACE program, and the PACE obligation will remain outstanding, the appraiser must analyze and report the impact on the value of the property, whether positive or negative, of the PACE -related improvements and any additional obligation (i.e., the PACE special assessment).

Home Equity Conversion Mortgages And Title I Loans

These policies are not applicable to Home Equity Conversion Mortgages (HECM) or Title I Loans. Properties with PACE obligations are not eligible for an FHA-insured HECM or Title I Loan.

Information Collection

The information collection requirements contained in this document have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB control number 2502-0059 and OMB Control number 2502-0538. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

Questions

Please address any questions about the topics addressed in this Mortgagee Letter to the FHA Resource Center at (800) 225-5342. Persons with hearing or speech impairments may reach this number via TTY by calling the Federal Relay Service at (800) 877-8339. For additional information on this Mortgagee Letter, please visit www.hud.gov/answers.

Signature

Edward L. Golding
Principal Deputy Assistant Secretary for Housing

Attachments
1, 2, 3, 4, 5, 6, 7, 8, 9, 10

(Download zip file)

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING-
FEDERAL HOUSING COMMISSIONER

Date: December 7, 2017

Mortgagee Letter 2017-18

To: All FHA-approved Mortgagees
All Direct Endorsement Underwriters
All FHA Roster Appraisers
All FHA Roster Inspectors
All FHA-approved 203(k) Consultants
All HUD-approved Housing Counselors
All HUD-approved Nonprofit Organizations
All Governmental Entity Participants
All Real Estate Brokers
All Closing Agents

Subject	Property Assessed Clean Energy (PACE)
Purpose	This Mortgagee Letter (ML) transmits revised policies for insuring mortgages secured by Single Family 1- 4 unit properties encumbered with Property Assessed Clean Energy (PACE) obligations.
Effective Date	This guidance is effective for case numbers issued thirty days after the date of this ML. All policy updates will be incorporated into a forthcoming update of the HUD Single Family Housing Policy Handbook 4000.1 (Handbook 4000.1).
Public Feedback	HUD welcomes feedback from interested parties for a period of 30 calendar days from the date of issuance. To provide feedback on this policy document, please send any feedback to the FHA Resource Center at answers@hud.gov. HUD will consider the feedback in determining the need for future updates.

Continued on next page

Affected Programs

This guidance applies to the origination of all FHA Title II forward mortgage programs, and the Home Equity Conversion Mortgage program (HECM).

Background

In ML 2016-11, FHA established requirements regarding the eligibility for FHA-insured mortgages of properties encumbered with PACE obligations that permitted, under some circumstances, a continuing obligation for repayment of the PACE obligation even after foreclosure and acquisition by FHA. These requirements were subsequently incorporated into the HUD Single Family Housing Policy Handbook 4000.1 (Handbook 4000.1).

FHA is concerned about the potential for increased losses to the Mutual Mortgage Insurance Fund due to the priority lien status given to such assessments in the case of default. FHA is also concerned with the lack of consumer protections associated with the origination of the PACE assessment, which are far less comprehensive than that of traditional mortgage financing products. FHA's involvement with accepting properties with PACE assessments may indirectly help to overshadow potential consumer abuses.

While the existence of FHA-insured financing for properties with PACE assessments creates additional choices for financing options, potential borrowers may face risk associated with the potential for property overvaluation due to the unknown or miscalculated effect of the PACE lien on the property value.

FHA is also aware of the need to provide guidance regarding the extinguishment of PACE obligations in association with forward mortgage refinances and HECMs.

Accordingly, FHA has revised its policies with respect to the insurance of mortgages on properties encumbered with PACE obligations.

The policies and procedures for the servicing of FHA-insured mortgages on properties encumbered with a PACE obligation as announced in ML 2016-06 are not impacted by this ML and remain in effect.

Summary of Changes

Attached to this ML are additions and revisions to the Handbook 4000.1. The following is a summary of policy changes, which is provided for informational purposes only.

Outstanding PACE Obligations

Properties encumbered with PACE obligations will no longer be eligible for FHA-insured forward mortgages.

Refinances

Clarification is provided to identify PACE obligations as existing debt that may be paid off using a Rate and Term Refinance.

Current policies allowing the use of a Cash-Out refinance to pay off PACE obligations remain unchanged.

HECMs

The existing prohibition of properties encumbered with PACE obligations remains unchanged for HECMs.

Clarification is provided to identify PACE obligations as Mandatory Obligations that must be paid off at closing, and may be paid off using HECM proceeds.

Single Family Policy Handbook 4000.1

The attached updates to HUD's Single Family Housing Policy Handbook 4000.1 will be incorporated in a future publication of the Handbook.

HECM Program

Properties which will remain encumbered with a PACE obligation are not eligible for an FHA-insured HECM.

The payoff of a PACE obligation is a Mandatory Obligation and it must be paid off at closing, and may be paid off using HECM proceeds.

Paperwork Reduction Act

The information collection requirements contained in this document are approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB control numbers 2502-0059 and 2502-0524. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to a collection of information unless the collection display a currently valid OMB control number.

Questions

For additional information on this ML, please visit www.hud.gov/answers or call FHA's Resource Center at 1-800-CALLFHA (1-800-225-5342). Persons with hearing or speech impairments may reach this number via TTY by calling the Federal Relay Service at 1-800-877-8339.

Signature

Dana T. Wade
General Deputy Assistant Secretary for Housing

Attachment

Article

PACE Loans: *Does Sale Value Reflect Improvements?*

Laurie S. Goodman and Jun Zhu

The Journal of Structured Finance Winter 2016, 21 (4) 6-14; DOI: https://doi.org/10.3905/jsf.2016.21.4.006

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Abstract

This article determines how the resale value of homes with PACE (Property-Assessed Clean Energy) improvements and financing compare with similarly situated homes that have no PACE involvement. The authors use a number of different methodologies to show that the net impact of PACE on resale value of a home, after taking into account the cost of improvements, ranges from $199 to $8,882. Moreover, the premium for PACE homes purchased out of foreclosure was closer to the higher end of the range. They conclude that a home with a subordinate PACE loan will provide collateral for FHA and GSE recoveries in a foreclosure sale that is at least as high as comparable properties without PACE improvements.

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FHA Clarifies Financing on Properties with PACE Loans

Laurie Goodman

July 2016

Property-Assessed Clean Energy (PACE) loans can be taken out to finance energy-efficient upgrades, including solar panels, energy-efficient air conditioning, new windows, insulation, or a water conservation system. Under current rules, residential PACE improvements are typically assessed with property taxes and have a lien priority on par with tax liens, placing them above other liens that may be on the property, including the first mortgage. The structure of this financing has historically limited the use of the program, as the Federal Housing Finance Agency (FHFA), the regulator of the government-sponsored enterprises (GSEs) has prohibited these institutions from purchasing or guaranteeing mortgages with a PACE loan attached. The Federal Housing Administration (FHA) has also been reluctant to make loans on homes with a senior PACE lien. Some PACE loan providers have made it clear that they are willing to subordinate the PACE lien, as long as the lien can travel with the property.

On August 24, 2015, FHA stated that it would make financing available for single-family homes with existing subordinated PACE loans, as long as certain conditions are met. On July 19, 2016, as part of the Clean Energy Savings for All Americans Initiative—a cross-government partnership involving the US Departments of Agriculture, Energy, Health and Human Services, Housing and Urban Development (HUD), and Veteran's Affairs, as well as the Environmental Protection Agency, designed to increase access to solar energy and promote energy efficiency—HUD clarified the conditions under which properties with PACE assessments can be purchased and refinanced with FHA loans. The Veteran Administration will also allow properties with PACE assessments to be purchased and refinanced with Veterans Affairs loans.[1]

The most important condition for allowing a home with existing PACE financing to obtain an FHA-insured loan is that the PACE lien be subordinated but be permitted to travel with the property—that is, it can be transferred from one property owner to the next, including through a foreclosure sale. In addition, to protect the successive property owner, the PACE obligation must be readily apparent to mortgagees, appraisers, borrowers, and other parties to an FHA-insured mortgage transaction, and information on PACE obligations must be readily available for review in the public records where the property is located.[2] Finally, to gather further information about how these loans affect the property's value, the appraiser must analyze and report on the impact of PACE-related improvements to the property's value.[3]

This is a huge step forward: it is the first time any government agency has agreed to insure or guarantee properties with PACE loans. Resolving the regulatory uncertainty by allowing subordinate liens to travel

with the property should pave the way for an increased volume of energy-efficient improvements. Requiring the PACE lien to be subordinate to the FHA mortgage protects the FHA; allowing the lien to travel with the property is important to encourage the product's use.

It is critical to the PACE market that the lien travel with the property for two reasons. First, many consumers are unsure how long they will be in a home and may be more reluctant to purchase a more expensive and more efficient product if it must be paid off when the home is sold. Energy-efficient enhancements benefit both consumers and society, and it is in the public interest to encourage these enhancements. Second, PACE loans are an emerging asset class; the loans cannot be made unless investors are willing to hold them. The loans will clearly trade better, especially in securitization form, if they can travel with the property, resulting in better rates and greater credit availability for consumers. If the lien was extinguished during foreclosure, it would affect the pricing on these instruments to the borrower.

FHFA Status on PACE Assessments

The FHFA has sent mixed signals on whether they can be comfortable with subordinate PACE loans on the same terms as the FHA. On one hand, the FHFA has indicated it is comfortable with Vermont legislation: the lien is subordinated to all liens on the property that exist when the PACE loan is filed and to all first mortgages recorded after the PACE loan, but the lien is permitted to run with the property. This statute did include a reserve fund to protect against losses because of foreclosure. On the other hand, recent statements by the FHFA suggest discomfort with having an assessment traveling with the property under any circumstances. For example, in June 2016, Alfred Pollard, general counsel of the FHFA, testified before the California legislature raising two concerns. First, even if the lien is subordinated, it is not really subordinate if it is not extinguished through foreclosure and is permitted to travel with the property. Second, PACE loans do not follow the same consumer protection requirements applicable to residential mortgage lenders (Pollard 2016). This short note addresses both issues.

The Effect of PACE Improvements on Property Value

The issue from the FHFA's point of view is that they believe if a GSE loan with a PACE lien goes to foreclosure and the lien travels with the property, the FHFA will receive less in proceeds than if the home did not have the improvements or the assessment. This argument assumes that the value of the property does not increase enough to offset the lien. In fact, in an empirical study I did with Jun Zhu, published in the *Journal of Structured Finance*, we show that energy-efficient improvements increase the value of the property by more than the PACE assessment (Goodman and Zhu 2016).[4]

We used data from Renovate America, the largest provider of PACE loans in California, with roughly an 80 percent share of that market. The California market is the largest for PACE improvements in the nation.

The data included all 773 loans on which Renovate America had financed an improvement and the home was later sold. The homes were purchased as early as 1976, the PACE improvement was made after Renovate America entered the market in 2011, and the home was sold between 2012 and mid-2015.

We used three methodologies in our analysis. First, we compared the sales prices on homes with PACE assessments (taking the project's costs into account) with the prices on those that would be predicted by home price indices based on the zip code and original purchase date of those homes. Depending on the index, we found the homes' resale value demonstrated a positive PACE premium of $199 to $8,882.

We also compared the PACE home with a matched sample of loans in the same zip code that had homes purchased and sold at the same time. The matched sample was randomly selected from loans that met the criteria. The gain on the PACE homes was $5,010 more than the gain on the non-PACE loans. Furthermore, 92 percent of the PACE loans had a sales price (adjusted for the PACE assessment) higher than the purchase price, versus 87 percent of the non-PACE sample.

Finally, we pooled the PACE loans with the matched sample and ran regressions, controlling for characteristics such as purchase price, square feet of living space, number of baths, and whether the property had a PACE loan. The regression coefficient on the PACE loan indicates that after netting out the assessment, the energy-efficient improvement added $4,042 to the sales price.

Regardless of methodology, we found the PACE improvement more than offset the cost by $199 to $8,882. Homeowners can more than fully recover their full costs at resale, whereas most other home improvements can recover only about 60 percent. While we have few data points on the sale price of homes that went into foreclosure with PACE improvements (the source of FHFA concern), many homeowners opt for a PACE-financed energy-efficient improvement when the original equipment breaks. These borrowers are willing to invest in their homes, rather than opt for a less good, more inexpensive fix or none at all, suggesting they are less likely to go to foreclosure. And if they do go to foreclosure, the correct comparison is the home with the improved collateral versus the unimproved foreclosed home, which may have broken equipment.

Consumer Protections

The second point Pollard made in his California testimony is that PACE loans are not subject to the same level of consumer protections that other mortgage loans have, such as the ability-to-repay tests. The ability-to-repay rule ensures mortgage products are standard: rates are fixed for at least five years, no interest only loans, no loans with prepayment penalties, and so on. (There are no debt-to-income restrictions on GSE loans.) And all PACE loans are fixed rate with terms of five years or more, are fully amortizing, and have no prepayment penalties. These loans are more stringent than the ability-to-repay rules in that PACE loans

limit the assessment term to the useful life of the improvement. Moreover, there is some underwriting on the borrower: typically he or she must be current on property taxes and cannot have had more than one late payment over the previous three years, and must be current on all mortgage debt and cannot have had more than one late payment over the previous 12 months. The property cannot have any federal or state income tax liens, judgment liens, or mechanic's liens. The borrower cannot have been involved in a bankruptcy proceeding during the previous two to seven years, depending on the area.

More importantly, many PACE loans have other consumer protections that matter for this type of home improvement product: restrictions to make sure the improvement costs are not so large relative to the home that the value cannot be recaptured, assurances that the contractor is legitimate, the contractor's fees are reasonable for the work done, and assurances that the work is completed in a satisfactory manner. In the Renovate America product, assessments originated before January 1, 2015, cannot be more than 10 percent of a property's value, 15 percent for most assessments originated after January 1, 2015. Mortgage debt cannot be more than 90 percent of a property's value before the assessment, 100 percent afterward. Most PACE loan providers require that the contractors be licensed, bonded, and insured. Projects are subject to a maximum finance amount across all major product types, and projects quoted beyond the ranges require special approval. The PACE provider does not pay the contractor until the homeowners sign a certificate assuring satisfactory project completion. The contractor must also ensure the proper permits have been obtained for the improvements.

We applaud HUD for embracing the PACE product in a manner that protects HUD and encourages homeowners to employ energy-efficient enhancements to their home by allowing the lien to travel with the property. We hope the FHFA allows the GSEs to make loans on properties with a PACE assessment on roughly similar terms, as we believe the GSEs would be at least as well off by making a loan on a home with an energy-efficient improvement and a PACE assessment as it would be in making a loan on a home that did not have the improvement or assessment.

Notes

1. Office of the Press Secretary, "Fact Sheet: Obama Administration Announces Clean Energy Savings for All Americans Initiative," news release, July 19, 2016, https://www.whitehouse.gov/the-press-office/2016/07/19/fact-sheet-obama-administration-announces-clean-energy-savings-all.
2. Brian Sullivan, "FHA to Insure Mortgages on Certain Properties with PACE Assessments," news release, July 19, 2016, http://portal.hud.gov/hudportal/HUD?src=/press/press_releases_media_advisories/2016/HUDNo_16-110.
3. Edward Golding, "Property Assessed Clean Energy (PACE)," Mortgagee Letter 2016-11, US Department of Housing and Urban Development, July 19, 2016, http://portal.hud.gov/hudportal/documents/huddoc?id=16-11ml.pdf.
4. The research conducted by the author and later published in the *Journal of Structured Finance* was funded by Renovate America and was not a product of the Urban Institute.

References

Goodman, Laurie S., and Jun Zhu. 2016. "PACE Loans: Does Sale Value Reflect Improvements?" *Journal of Structured Finance* 21 (4): 6–14. http://www.iinews.com/site/pdfs/JSF_Winter_2016_PACENation.pdf.

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