Appraisal Institute®

Professionals Providing Real Estate Solutions

March 16, 2020

Federal Housing Finance Agency
400 7th Street SW
Eighth Floor
Washington, DC 20219

Re: PACE Request for Input, Notice No. 2020-N-1

To Whom It May Concern:

On behalf of the more than 17,000 members of the largest organization of professional real estate appraisers, we thank you for the opportunity to comment on the Federal Housing Finance Agency's ("FHFA") Request for Input ("Request") relating to residential Property Assessed Clean Energy (''PACE'') financing.

The Appraisal Institute has several high-level concerns with the way in which PACE programs are financed and complications that are created for appraisers in the appraisal process, including:

- PACE programs do not have safety guidelines in place that would protect homeowners from obtaining mortgage loans for more than the property is worth. Most of the programs that we have seen do not require an appraisal because the lien runs with the property. We firmly believe that significantly enhanced buyer protections need to be in place for PACE programs to succeed. Thus far, we have heard far too many stories of abuse with the program.
- Full disclosures are currently not always being made by the real estate agents involved in a sale to the consumer(s) involved in the sale of the property. Furthermore, any potential lack of disclosure to the appraiser is unacceptable and has the potential to distort the results of the appraisal process.
- Homeowners with existing mortgages are not required to notify their lender that a PACE loan has been taken, and therefore, the tax bill will be dramatically increased to cover the PACE annual payment. If the mortgage payment includes principle, interest, taxes, and insurance but didn't allow for the increased tax bill because of the PACE payment, will the homeowner have the funds to make the extra payment? If a mortgage exists on the property, the PACE program should be required to notify the mortgage company immediately to resolve any issues regarding additional tax consequences and mortgage position. (Fannie Mae, Freddie Mac, and FHA will not accept second position to this kind of PACE program.)
- Lenders should be asking title companies to search for PACE Assessments prior to the loan's closing. If title companies do not search for a PACE Assessment, and one is subsequently discovered, the consumer could end up not being able to finance the property, and the real estate agent, appraiser and title company could face a lawsuit for negligence.
- PACE programs are not always at interest rates that are competitive with mortgage rates. In some cases, property owners would be better served by refinancing their homes and rolling the cost of solar into their mortgage.

Appraisal Process

The existence of a PACE loan is comparable with situations that involve a special assessment for sewer or water. The special assessment can pass to the new buyer or be paid off by the seller. The sale price paid is negotiated based on who assumes the special assessment.

From a valuation perspective, it is important to understand whether a seller paid assessment influenced the sales price. This is best understood by comparing sales with a PACE Loan or Special Assessment to a sale without one. This comparison quickly reveals if the assessment affected the price paid.

This is likely a form of sales or seller concession, and if so, recognized appraisal methodology would deduct this concession dollar for dollar under a “cash equivalency” basis, or if the market suggests the amount is less than market based on a paired sales analysis, the market-derived adjustment would be applied.

The example found at Table 1 below illustrates how the appraisal industry analyzes this type of situation. The appraiser would consider the PACE loan and how it was handled in the sale. If the buyer assumed the PACE Loan as in Sale 1, this amount would have to be considered in the market conditions adjustment because the borrower actually paid $185,000 and not $175,000. Sale 2’s example shows that when the seller pays off the PACE loan, the property sells for more than Sale 1’s price that is usually reported in the MLS. The difficulty and risk in these types of sales where the borrower assumes the PACE loan requires the appraiser to have access to the amount assumed and it should be clearly shown in the MLS. A prudent buyer will discount the price paid based on the amount of the PACE loan they would have to assume. And if they could not receive a mortgage because of the PACE loan taking first position, only buyers with cash or private financing would qualify. This is where the problem lies in disclosure. Agents often report they aren’t aware of the PACE until closing and often is not reported in the MLS. It should be noted that there are no absolutes, and every situation is different, since every real estate market is different. However, this is likely to be a common scenario. This scenario is a typical occurrence in the City of Cape Coral, FL where some properties have special water and sewer assessments up to $16,000. Appraisers use the paired sales analysis shown below to develop adjustments.

Table 1

	Sale 1	**Sale 2**
Sale Price	$175,000	$185,000
Concessions	Buyer assumed the PACE loan for utility connection	Seller paid off the $10,000 PACE Loan for utility connection
Financing	Conventional mortgage	Conventional Mortgage
Date of contract	7/2/2017	7/31/2017
Energy Efficiency	Good – HERS 55	Good- HERS 58

Of course, the positive impacts of the any fixed improvements or features of the property would also be analyzed by an appraiser. This includes cost and income considerations as discussed above in the description of appraiser considerations and the three approaches to value.

It is here – the application of the income capitalization approach - where we believe lenders, encouraging analysis by appraisers can potentially resolve several areas of concern with regard to the PACE program, particularly as it relates to solar integration. The lack of disclosure in public record will be a problem for automated valuation models (AVMs) that will pick up only a part of the transaction and not the full amount the borrower paid.

We believe the appraiser should receive proper disclosures at the onset of a potential appraisal assignment for a mortgage loan, including who is to assume the PACE or Utility Loan and the amount of the remaining balance of the loan. Comparable sales with PACE loans (where the buyer assumed the PACE loan) likely requires an adjustment when an appraiser uses that sale as a comparable to a property that is unaffected by a PACE loan. Therefore, the amount assumed must be properly disclosed in applicable real estate sales data sources available to appraisers to allow the appraiser the opportunity to analyze those sales to determine if the sale price was affected by the loan assumed.

Finally, we have observed the PACE lien being called different names. For instance, in California it is called Home Energy Renovation Opportunity (HERO). Changing the name to avoid the negative consequences that might occur if the real estate agent or appraiser was not familiar with the name further complicates this issue.

Should you have any questions or need additional information, please contact Bill Garber, Director of Government and External Relations, Appraisal Institute, at 202-298-5586 or bgarber@appraisalinstitute.org, or Brian Rodgers, Manager of Federal Affairs, Appraisal Institute, at 202-298-5597 or brodgers@appraisalinstitute.org.

Sincerely,

Appraisal Institute