Comments of the California Law-Income Consumers Coalition on PACE Request for Input, Notice No. 2020–N–1

March 16, 2020

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

Dear Sir or Madam:

Please see the submission below in response to the Federal Housing Finance Agency (“FHFA”) Request for Input (“RFI”) to solicit information relating to residential Property Assessed Clean Energy (“PACE”) financing (Notice No. 2020–N–1). Many of the below signatories have experience in enforcement of consumer protection laws, as well as direct experience representing individuals impacted by the absence of consumer protection laws for PACE loans. We are also legal academics who research and teach about consumer protection law and consumer advocates on behalf of low-income consumers in California. We appreciate the opportunity to submit these comments for your consideration.

California Low-Income Consumer Coalition:
Bet Tzedek Legal Services
Centro Legal de La Raza
East Bay Community Law Center
Elder Law & Advocacy – San Diego
Justice & Diversity Center – San Francisco
Legal Aid of Marin
Legal Aid Society of San Bernardino
Public Counsel – Los Angeles
Public Law Center of Orange County
Riverside Legal Aid
Santa Clara U. – Alexander Community Law Clinic
UC Irvine – Consumer Law Clinic on behalf of their clients
Watsonville Law Center

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? By how much should available loan-to-value ratios be reduced to address the increased risk of such liens being placed on the property and what related implications would result from such actions? Should loan-to-value (LTV) ratios be reduced for all loan purchases sufficient to take into account the maximum amount of a PACE financing available in that community? Should potential future increases in permitted percentage of available PACE financing-to-assessed value be considered?

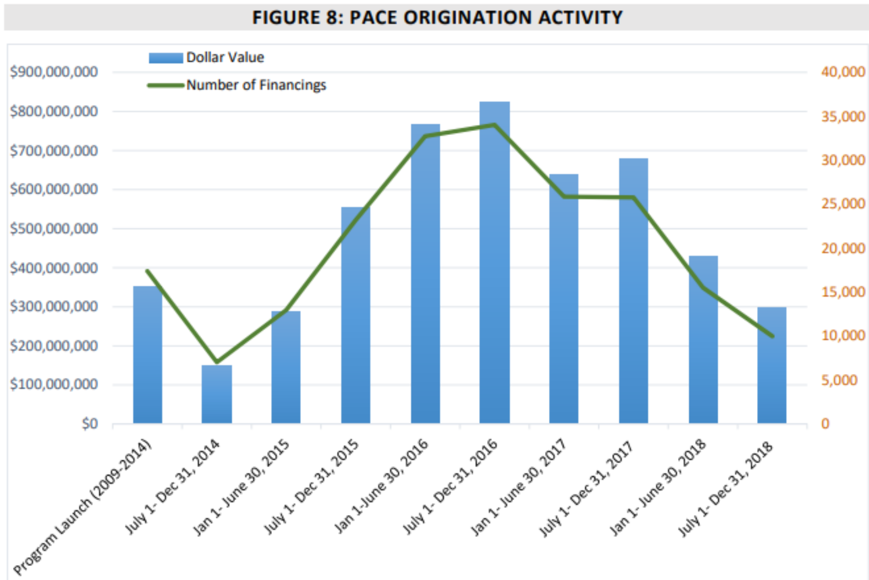
CLICC agrees in full with the comments submitted by the National Consumer Law Center and National Housing Law Project ("NCLC Comments") as to this point. We believe that decreasing LTV ratios would be a drastic step that would harm all consumers in a state with the most harm falling on the most vulnerable consumers. Additionally, the costs of this policy would outweigh any benefit to lenders. First, lowering LTV ratios does not provide any additional insurance for lenders, who are already protected by the California Loss Reserve Program. Second, the administrative burden of tracking which communities participate in the PACE program would be unduly burdensome. Third, as explained in the NCLC Comments, lowering LTV ratios would unnecessarily restrict access to credit for communities simply because PACE has been authorized.

The FHFA need not decrease LTV ratios because there are programs in place to compensate mortgage lenders for losses incurred as a result of PACE. In June of 2014, the California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA) launched the California Loss Reserve Program. The goal of the program is to put first mortgage lenders in the same position they would be in without the PACE lien on the property by making the first mortgage lenders whole for any direct losses incurred due to the existence of a PACE lien on a property.[1] Senate Bill 96 (Committee on Budget and Fiscal Review, Chapter 356, Statutes of 2013) authorized CAEATFA to develop and administer the PACE Loss Reserve Program with an initial allocation of $10 million. To date, CAEATFA has not received any claims on the loss reserve.[2] The existence of the loss reserve program makes any restrictive LTV policy unnecessary for at least another eight to twelve years based upon current projections.[3] It should also be noted that PACE origination activity in California is on a decline as shown in the graph below:

[1] 2018 Annual Report to the California Legislature, CALIFORINAI ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION FINANCING AUTHORITY at 19 (March 2019) available at https://www.treasurer.ca.gov/caeatfa/annual/2018.pdf

[2] See https://www.treasurer.ca.gov/caeatfa/pace/activity.asp

[3] *Supra* note 1 at 21



[4]

Second, tailoring an LTV policy to account for the possibility of PACE assessments would require the FHFA to track municipalities that enroll in PACE. PACE enrollment which can be at a county or municipal level, with confusing and overlapping rules within jurisdictions. For example, only eight out of twenty municipalities within Orange County, California have authorized PACE, while Los Angeles has both a county-wide program and specific municipal programs within the county. The suggested LTV policy would also requiring continual tracking of those programs as some PACE Authorities have withdrawn from the program such as Kern County, CA and Bakersfield, CA.[5] Although CLICC strongly believes that more sophisticated data collection and tracking is needed within the PACE program, this LTV policy would involve significant administrative burdens that outweigh the benefits of the policy to the FHFA, the Enterprises, or to consumers.

Finally, lowering LTV ratios is an overbroad and unnecessarily restrictive response to the PACE problem. Lowering LTV values would only reduce access to credit for lower income borrowers who may lack the ability to provide higher down payments. In addition to being harmful for lower income individuals, this policy is disproportionate to the problem it attempts to remedy. California saw 25,513 new PACE assessments in 2018—less than 4% of the number of mortgages originated that year.[6] As already established, this cost would come at little added protection for lenders. Thus, lowering LTV ratios amounts to an essentially punitive measure for entire communities that feature PACE—punitive measures that will hit vulnerable communities

[4] *Supra* note 1 at 21

[5] James Burger, " 'I see this as putting our communities at risk.' Kern County Board of Supervisors votes to end PACE Program," June 14, 2017, available at http://www.tehachapinews.com/news/i-see-this-as-putting-our-communities-at-risk-kern/article_5f216698-5132- 11e7-a4d2-236c7d03e2f3.html and Steven Mayer, "Bakersfield City Council ends PACE loan program," Jul. 19, 2017, available at http://www.bakersfield.com/news/bakersfieldcity- council-ends-pace-loan-program/article_e33cc8b0-6cfc-11e7-b4b9-4775b9e99903.html).

[6] CAEFTA "PACE Loss Reserve Program Enrollment Activity"; First Tuesday, "California's Annual Mortgage Report Card is Out," https://journal.firsttuesday.us/californias-annual-mortgage-report-card-is-out/69442/

the hardest—even though most of the members of that community likely will not participate in PACE.

2. Should FHFA direct the Enterprises to increase their Loan Level Price Adjustments (LLPAs) or require other credit enhancements for mortgage loans or refinancings in communities with available PACE financing? What increased levels would be appropriate for such LLPAs in light of the risks of PACE financing posed to the Enterprises?

For the reasons articulated in the answer above, and in the NCLC Comments, FHFA should not direct the Enterprises to increase their LLPAs or require other credit enhancements for mortgage loans or re-finances in communities that have authorized PACE financing. Imposing a greater LLPA or requiring other credit enhancements would increase costs for borrowers, with the costs having the greatest effect on the most vulnerable borrowers. Increasing LLPAs would be an additional roadblock, in particular low-income individuals, looking to purchase a home in the area and would unnecessarily penalize them though they may never obtain a PACE assessment.

3. Should FHFA consider other actions regarding Enterprise purchase or servicing requirements in jurisdictions with PACE programs?

As discussed above, there is no need to modify Enterprise purchase requirements in jurisdictions with PACE programs. However, CLICC agrees with the NCLC Comments that FHFA should direct Enterprise servicers to take proactive steps and develop protocols. Those outlined in the NCLC Comments would have the dual effects of protecting the Enterprises and protecting the most vulnerable consumers.

First, servicers should be required to carefully monitor the tax bills to detect when a PACE Assessment has been added to the property tax bill. If there is a significant increase in the property tax bill, the servicer should be required to look at the bill itself to determine if a PACE assessment has been added. In California, the taxing authority adds a line item to the tax bill to reflect the assessment. Though not all taxing authorities use the same terminology, the line items are easily identifiable under the Special Assessment Charges on the face of the bill by usage of "Clean Energy", by the PACE program name such as "CA HERO PGM-CLEAN ENERGY-RESIDENTIAL" or "PACEFUNDING OPEN PACE PROGRAM".

Homeowners should also be given the option to voluntarily make higher payments escrow payments in anticipation of the first PACE Assessment tax payment becoming due similar to when servicer anticipates a substantial increase in disbursements from the escrow account after the first year of the loan.[7] This could be similarly implemented on properties in which there is a PACE assessment.

A recurring problem for vulnerable consumers in California has been a high degree of fraud surrounding PACE transactions. Members of CLICC have spoken to countless homeowners who were told that PACE was a free government program and who only learn about their payment

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[7] 12CFR § 1024.17(a)

obligations when they receive a higher tax or mortgage bill. This is another area where a timely notification from a mortgage servicer could serve to protect the interests of both the Enterprise and the consumer. The notice to borrowers regarding PACE should include information about how to contest PACE assessments should the borrowers believe that they are erroneous or invalid. If borrowers demonstrate that they are disputing PACE assessments with their PACE administrator or taxing jurisdiction, Enterprise servicers should delay payment of PACE assessments and/or incorporation of PACE assessments into regular escrow payments.

Such guidance is needed because our client experience shows that notifying the servicer is ineffective in allowing for voluntary payments, which is highly problematic given the time in which it takes for the first PACE assessment to come due and the significant amount of the payment. For example, if a PACE Assessment lien is recorded on July 1, 2020, the first tax bill to reflect the assessment will not be sent until October 2021 and will not be due until November of 2021. Depending upon when the escrow account computation year ends, an escrow account analysis will not notify a borrower of the increase for up to a year afterwards requiring the homeowner to not only adjust their payments for the ongoing increased property tax amount but also to make up for any shortages.

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? How might those standards best address the increased risk of such collateral? Should such standards be in line with actions that FHFA would undertake for the Enterprises, recognizing the difference in business structures between the Enterprises and the Banks?

As described above and in the NCLC Comments, establishing safety and soundness standards from Federal Home Loan Banks (FHLB) in PACE districts would do nothing more than limit the availability of credit for very-low, low- and moderate-income borrowers that benefit from the program. Such limitations are unwarranted as they offer little additional protections and is contrary to the FHLB's managements' assessment of the need for enhanced standards.[8]

5. How might the Enterprises best gather or receive information on their existing guaranteed or owned mortgage loan portfolios 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 Enterprises on a periodic basis? What would the costs and implications be of such a requirement?

We agree with the NCLC Comments that any servicer notification requirement should be placed on PACE program administrators or local government sponsors, not homeowners. Some PACE administrators already have provisions speaking to notification requirements. For example, Ygrene's Unanimous Approval Agreement states

> "The Owner authorizes the Program to send a Notice to Lender of Proposed Special Tax to each mortgage lender that holds a note or alternative debt instrument secured by a lien on the

[8] Federal Home Loan Banks Office of Finance Lending and Collateral Q&A (Nov. 13, 2019)

Property (the "Notice"). It will notify lenders that the Owner intends to authorize the recordation of a Notice of Special Tax Lien against the Property."

Mortgage servicers should be required to gather and report to the Enterprises what properties have a PACE assessment, the amount of escrow shortages, and mortgage performance data on a semi-annual basis to allow for better tracking of the impact of PACE assessments.

6. Would it be most effective 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? What data should be included in such a registry? What access would be permitted while protecting consumer privacy? Should a federal agency provide for such a registry? What minimum information would be available to allow credit reporting agencies to include PACE obligations in credit reports obtained in connection with mortgage origination or servicing?

CLICC agrees in full with the NCLC Comments on this point. We write to clarify the current but disparate efforts underway to create PACE registries, and to call for a consolidated system, accessible by all stakeholders including FHFA and the Enterprises along with other state and federal regulators. We believe this registry should be maintained by the Consumer Financial Protection Bureau ("CFPB").

First, it should be noted that California already requires various reporting and/or registries by the PACE programs. Currently, the California Alternative Energy and Advanced Transportation Financing Authority (CAEAFTA) collects information from enrolled PACE programs. In order to participate in the Loss Reserve Program, a PACE Program must submit an application, including formation documents, underwriting criteria, transactional costs, credit enhancements, and the total number and value of the existing portfolio.[9] CAEAFTA also collects additional information from enrolled PACE programs in required semi-annual reports including the assessor's parcel number, principal amount, annual assessed amount, and term of each new financing originated in the reporting period.[10]

As of January 1, 2019, the Department of Business Oversight began licensing Property Assessed Clean Energy (PACE) program administrators and regulating the PACE industry.[11] Though the PACE regulations have yet to be issued, the DBO has begun maintaining a registry of PACE solicitors and solicitor agents.

There remains a need for a real time registry in order to prevent one property from having multiple PACE Assessments simultaneously, a practice some PACE solicitors (i.e. home improvement contractors) employ to increase the available financing. In February 2020, during a recent DBO Stakeholders meeting, the PACE Administrators indicated they have developed a registry to prevent this practice and hold PACE Solicitors more accountable. However, the registry is not publicly available, nor does it provide all of the information that would allow for

[9] 4 CA ADC § 10081
[10] 4 CA ADC § 10085
[11] CA AB 1284 (Chapter 475, Statutes of 2017).

careful monitoring and enforcement of PACE statutory requirements.

To be more effective, the registry should provide more comprehensive information such as the fair market value of the property used to determine eligibility, loan to value amount including the PACE assessment, date of origination and amount, payment schedule, and loan terms. These disclosures are not burdensome to the PACE administrators because this information is already required by statute.[12]

The DBO and/or CAEAFTA could provide for a more robust registry as outlined above, but it would still be limited to California. It would be in the best interest of the consumers and FHFA to have a registry is publicly available and standardized on a national scale, accessible by all interested stakeholders including FHFA and the Enterprises. Since the CFPB has already been authorized to develop PACE ability to pay standards, and will continue to monitor and enforce ability to pay standards, the CFPB is in the best position to provide a national registry and standardize that registry for everyone across the nation.

One final note is credit reporting agencies should not be allowed to include PACE assessments on credit reports as they are non-recourse loans.

7. Should servicers of mortgage loans for the Enterprises provide an annual or more frequent notice to existing borrowers in PACE-eligible communities informing them that, under the terms of their mortgage, PACE liens are not permitted? Should borrowers be informed of the difficulties that may arise in selling or refinancing their home when a PACE lien has been placed on their property? What other information, if any, should be provided by servicers to borrowers with regard to PACE liens? Should borrowers in PACE jurisdictions be required to execute any additional agreements or certifications in connection with mortgages for the Enterprises, Home Loan Banks or FHA guaranteeing the borrowers will not accept PACE financing for energy efficiency improvements?

An annual notice, more frequent notices, or any additional agreements or certifications "guaranteeing" that they will not accept PACE Financing to borrowers in PACE-eligible communities will provide no additional protections to the Enterprise while creating an additional administrative burden. Nor do notice requirements provide a meaningful protection to consumers because, in reality, people do not read consumer disclosures. A study published in the Annual Review of Economics by Loewenstein, Sunstein, and Golman found that fewer than 3% of consumers read the privacy disclosures on websites.[13] In 2014 the Stanford Law Review published an article which discussed how people do not read important parts of one-time contracts such as home mortgage assessments.[14] Furthermore, PACE contractors tend to target older adults and aging individuals, and studies have found that financial literacy scores decline by about 1% per year after the age 60.[15] Thus, older adults have a heightened vulnerability to

[12] California Financial Code FIN CA FIN Section 22684
[13] Loewenstein, George, Cass R. Sunstein, and Russell Golman, *Disclosure: Psychology Changes Everything. Annual Review of Economics* (2014)
[14] Kleinmann Commc'n Grp., Inc., *Know Before You Owe: Evolution of the Integrated TILA-RESPA Disclosures* (2012)
[15] Gamble, Keith J, et al. *How Does Aging Affect Financial Decision Making? Center for Retirement Research* (2015)

advertising fraud.[16] Therefore, there is a large possibility that most homeowners will not read these occasional notices from the Enterprises.

Notice should be provided to the consumer at the time they are being solicited for a PACE assessment. However, the FHFA cannot do this because the FHFA does not know when the PACE assessments are being originated. Therefore, the PACE administrators should be responsible to provide this notice to the consumer at the time of origination when the consumer can make a meaningful step to protect themselves by having the option to cancel the PACE assessment. Current notice requirements are insufficient and do not allow sufficient time for the consumers to verify the PACE implications with their mortgage servicers. For these reasons, FHFA should use their authority and influence within home financing to encourage additional consumer protections through the Consumer Financial Protection Bureau's rulemaking process.

8. The Consumer Financial Protection Bureau published and received comment on an Advanced Notice of Proposed Rulemaking on disclosures under the Truth in Lending Act, as required by section 307 of the Economic Growth, Regulatory Relief and Consumer Protection Act, Public Law 115–174 (2018). The ANPR addresses, in line with the statute, TILA sections relating to ability to repay requirements and to application of civil money penalty provisions for TILA violations. FHFA seeks input on matters beyond the scope of the statutory and regulatory provisions addressed by the CFPB. For example, do consumers face issues regarding the tax treatment of PACE loan payments and reporting to consumers of deductible versus nondeductible expenses? Are there consumer impacts from PACE liens on title searches? What impacts might arise where local governments use structures such as an unelected Joint Powers Authority that limit government responsibility for PACE program administration? What options exist for a homeowner who can no longer afford to repay a PACE lien, such as a tax deferral by the taxing authority? What issues arise from the use of approved contractor lists and the impact on costs, contractor regulation, and recourse for consumers for defective equipment? What issues may arise from notification practices regarding PACE liens at time of property sales and other issues that align with or expand on consumer related concerns raised by the CFPB?

We believe the CFPB has the authority under TILA to regulate PACE lending beyond the two matters specified within this question. The CFPB's PACE ability to repay ("ATR") requirements should trigger remedies under Sections 1640 and 1641 of TILA. While remedies vary depending on which provision of TILA applies, for the ATR rule, remedies include statutory and actual damages, enhanced damages, attorneys fees and costs. Ensuring these remedies are essential to promote rule compliance and to ensure harmed consumers are properly compensated. The Bureau should also apply TILA and Regulation Z disclosure and servicing requirements.

We agree with the NCLC Comments that the CFPB is best positioned to protect vulnerable homeowners from abuses within the PACE industry. As explained above, we believe doing so will have the added benefit of mitigating risks to the Enterprises.

[16] Denburg N. L., Cole C. A., Hernandez M., Yamada T. H., Tranel D., Bechara A., et al, *The orbitofrontal cortex, real-world decision making, and normal aging*, Ann. N. Y. Acad. Sci. 1121 480–498 (2007)

To the extent the CFPB's rulemaking authority may not extend to title searches and tax treatment, the experience of California advocates is that these are issues for consumers.

While we are not aware of any widespread study on the impact on consumers from PACE liens on title searches, we have heard anecdotally from real estate agents that PACE liens on title searches are most often discovered toward the end of a real estate transaction, and in many cases derail that transaction altogether, impacting the buyer, seller, and agent.

Very few options exist for a homeowner who can no longer afford to repay a PACE lien, particularly if they have an impound/escrow account. We have seen a few examples of successful refinancing, but in most cases the borrower will be denied either for lack of credit or because the lender would require payoff of the PACE lien, depriving the borrower of significant equity in most cases (for a PACE loan with terms they often dispute having agreed to). In small percentage of cases, and as may be permitted by the loan documents, if a bona fide dispute exists as to the validity of the PACE loan, a mortgage servicer may permit the borrower to set aside the PACE loan portion of their escrow payment until the dispute is resolved. Almost always, however, such requests are denied. Furthermore, by the terms of the PACE assessment, the taxing authority is not permitted to authorize a tax deferral on a PACE lien, and in fact is obligated to accelerate foreclosure upon request by the PACE administrators or their investors. Even taxing authorities that may permit partial payments are still required to immediately charge late fees and interest on the unpaid portions, compounding the debt and likelihood of default to the borrower.

These problems are compounded by the use by local governments of structures such as an unelected Joint Powers Authority that limit government responsibility for PACE program administration. We have heard from County taxing authorities, for example, that they have little more than ministerial authority over PACE assessments approved and submitted through JPAs, and lack the ability to remove or defer payment of a JPA-issued assessment. County-run programs have more autonomy, but often cede that autonomy through contracts with third party PACE administrators.

9. What information regarding experiences under programs of the Department of Housing and Urban Development relating to PACE may be relevant for consideration by FHFA in its evaluation of public input? Where PACE programs create super-priority liens, 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 or assignment claims or the availability or terms of modifications allowable? Should government programs, such as those of FHA, contemplate further limiting the availability of mortgage insurance in PACE jurisdictions for forwards, HECMS or both? Are there improvements that government programs could undertake, such as FHA increasing utilization of its "green" insured mortgages or its Section 203(k) rehabilitation mortgage insurance program to avoid the risks associated with PACE programs?

Making adjustments such as risk-based mortgage insurance premiums or limits on partial or assignment claims or the availability or terms of modifications allowable would impose additional costs and burdens for homeowners in PACE jurisdictions contrary to the goals of FHA, VA, and/or USDA/RA lending programs. Given that PACE solicitors often target low-income neighborhoods or the elderly, it would impose additional burdens on them simply because they are in PACE jurisdictions. Instead utilization of “green” insured mortgages or Section 203(k) rehabilitation mortgage insurance program to avoid the risks associated with PACE programs would be a better option for many homeowners in PACE jurisdictions.