National Association of Home Builders

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March 26, 2012

Mr. Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
400 7th Street, SW
Washington, DC 20024

Re: Advanced Notice of Proposed Rulemaking
Mortgage Assets Affected by PACE Programs
RIN 2590-AA53

Submitted via Electronic Delivery to:
RegComments@fhfa.gov

Dear Mr. Pollard,

On behalf of the National Association of Home Builders (NAHB), I appreciate the opportunity to respond to the Federal Housing Finance Agency's (FHFA) request for comments on the Advance Notice of Proposed Rulemaking (ANPR) on Mortgage Assets Affected by PACE Programs. FHFA's ANPR requests input on Property Assessed Clean Energy (PACE) programs and, more specifically, whether FHFA's restrictions and conditions on PACE programs should be maintained, changed or eliminated and whether other restrictions or conditions should be imposed.

NAHB is a Washington-based trade association representing more than 140,000 members involved in all aspects of single family and multifamily residential construction. NAHB and its members have a strong interest in supporting a housing finance system that offers home buyers access to affordable mortgage financing in all geographic areas in all economic conditions.

Background on Property Assessed Clean Energy (PACE) Programs

The Property Assessed Clean Energy (PACE) program was developed in 2008 to mitigate home owners' cost and financing impediments to the installation of energy efficient and renewable energy systems. A PACE lien is a financing option for home owners who want to live in a more energy efficient home, but either choose not to pay out-of-pocket for costly improvements or do not have the money to pay for the extensive retrofits that would provide the desired benefits of lower utility bills and energy conservation.

PACE liens generally are financed through bonds issued by a local jurisdiction. Home owners apply for PACE financing through their local government and repay the lien over time through a special assessment on their tax bills. The PACE-enabling legislation passed by most states calls for PACE liens to take a first-lien position and requires an existing mortgage loan to be subordinated to the PACE lien.

PACE eliminates the upfront payment for energy efficient improvements and makes the cost of the improvements more affordable to home owners by stretching out the repayment period over 10, 15 or 20 years. Since PACE financing is tied to the property and not the home owner, the home owner who makes the improvements to the home is not necessarily responsible for the entire cost of the improvements. If the home is sold prior to the PACE lien being paid in full, the payments on the lien become the obligation of the new home owner. As of January 2012, 27 states had passed legislation authorizing local governments to set up PACE and PACE-like programs and 20 more state legislatures and local governments were considering authorizing or implementing PACE programs.

Regulatory Actions on PACE Programs

On July 6, 2010, FHFA issued a *Statement on Certain Energy Retrofit Loan Programs* that said PACE lien programs "present significant risk to lenders and secondary market entities, may alter valuations for mortgage-backed securities and are not essential for successful programs to spur energy conservation." FHFA determined that first liens established by PACE liens "pose unusual and difficult risk management challenges for lenders, servicers and mortgage securities investors" and directed Fannie Mae, Freddie Mac and the Federal Home Loan Banks to undertake specific actions to address PACE programs with first-lien requirements.

The actions stipulated by FHFA effectively prohibited Fannie Mae and Freddie Mac (the Enterprises) from purchasing PACE liens with first-lien priority status. Even more significantly, to ensure a PACE lien is not added to the property without Fannie Mae or Freddie Mac's knowledge, Freddie Mac and Fannie Mae are prohibited from purchasing mortgages in any jurisdictions that allow PACE programs requiring first-lien status. Due to the predominant role Fannie Mae and Freddie Mac play as purchasers and securitizers of mortgage loans, the result of these FHFA-directed actions has been to shut down the availability of PACE financing in any municipality where it is structured as a first lien.

The same day FHFA issued its Statement, the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the National Credit Union Administration issued similar statements directing the institutions they supervise to consider the impact PACE financing may have on both current mortgage portfolios and ongoing mortgage lending activities.

On February 28, 2011, FHFA directed Fannie Mae and Freddie Mac to continue to refrain from purchasing mortgages secured by properties with outstanding first-lien PACE obligations and to continue to operate in accordance with Lender Letters issued by each Enterprise in August 2010 that detailed lender requirements to address risks and specified steps necessary to ensure their operations were protected from first-lien PACE programs.

Both Fannie Mae and Freddie Mac specifically advise their customers that neither Enterprise will purchase mortgages secured by properties subject to PACE obligations that require first-lien priority status. Both Enterprises emphasize to their customers that they are responsible for monitoring state and local laws to determine whether a jurisdiction has a PACE program that provides for first-lien priority.

NAHB Comments

NAHB is a long-standing proponent of energy efficient new homes and energy efficient retrofits in existing homes that offer home owners the benefit of lower utility payments and contribute to efforts to reduce energy consumption. NAHB recognizes that home owners often find the upfront costs to retrofit an existing home with energy efficient and renewable energy systems prohibitive and may forego energy efficient improvements due to uncertainty about whether they will own the home long enough to recoup their investment through energy savings. PACE programs address both of these home owner concerns.

NAHB believes it is important to support initiatives, such as PACE, that seek to finance energy efficient and renewable retrofits for residential and commercial properties. However, NAHB is concerned about the potential negative impact of first-lien PACE programs on the functioning of the housing finance system. Further, NAHB does not believe the PACE program is the right financing vehicle to assist property owners unless the financing is designed to include protections for consumers and eliminate the current safety and soundness risks for mortgage lenders, Fannie Mae, Freddie Mac, the Federal Home Loan Banks and the MBS market.

NAHB therefore believes the restrictions and conditions placed on PACE and PACE-like programs by FHFA should be maintained when these programs are structured in such a manner that a PACE lien takes a first-lien position ahead of a pre-existing mortgage loan or ahead of a new mortgage loan originated on a property with an outstanding PACE obligation. Such conditions undermine the safety and soundness of the secondary mortgage market and may alter valuations for mortgage-backed securities by increasing the severity of loss to the mortgage lender in the event a mortgage goes to foreclosure and the lender is obligated to pay past-due amounts outstanding on the PACE lien.

Impact to the Secondary Market

NAHB is very concerned about the impact to the secondary market if Fannie Mae and Freddie Mac were to purchase and securitize mortgage loans that are not in a first-lien position. Even more importantly, NAHB is concerned that PACE programs allow for a lien to be attached to a property after the mortgage loan has been originated and sold to Fannie Mae and Freddie Mac placing the mortgage loan in a second-lien position without the knowledge of either the Enterprise or the mortgage security investor.

A lack of transparency around the origination of PACE liens means there is the potential for these liens to encumber a property without the knowledge of the secondary market entities and investors. The possibility that this could occur would have a direct chilling effect on the liquidity of the mortgage securities market and decrease the value of mortgage investments. NAHB does not support financing programs that have the potential to disrupt the secondary mortgage markets, have a negative impact on the value of MBS, and increase the cost of mortgage borrowing.

Impact to the Consumer

NAHB believes allowing PACE liens to be structured as first liens not only jeopardizes the lender and the secondary markets but also renders the home owner in violation of his or her mortgage security instrument, i.e. in default, if the mortgage is owned by Fannie Mae or Freddie Mac. As PACE programs do not require the disclosure of this information to the home owner upon origination of the PACE lien, the home owner may be unaware that if the PACE financing were to become known to Fannie Mae or Freddie Mac, the mortgage loan would be immediately due and payable.

A home buyer who wants to purchase a home with a PACE first lien is at a disadvantage. Since the mortgage loan is not saleable to Fannie Mae or Freddie Mac, the home buyer may not be able to find a lender willing to make the mortgage. Potentially, the home cannot be sold or the sales price might be reduced by the amount necessary to pay off the PACE lien. In either instance one party is disadvantaged by the existence of the PACE lien and the value of the home is decreased. (The allowance of prepayments of PACE liens varies by state and program.)

NAHB Supports PACE Programs That Protect Home Owners and Do Not Require the PACE Lien to Have a First Lien Status

NAHB supports PACE programs that do not require the PACE financing to have a first-lien status and that incorporate a certain level of borrower underwriting and disclosures to protect home owners.

NAHB has members that specialize in installing energy efficient and renewable energy systems in residential and commercial properties. As an association, NAHB is supportive of as many avenues as possible for home owners to finance these improvements to their homes. However, it is critical the financing product does not impair the functioning of the housing finance system and offers home owners safe and sound products with a degree of underwriting and disclosure that ensures the home owner understands the product, can afford the payments and is not jeopardizing his or her ownership of the home in any way.

NAHB believes PACE liens should be designed, at a minimum, to include the safeguards for lenders, consumers, the secondary mortgage entities and MBS investors that are recommended in the *Guidelines for Pilot Pace Financing Programs* issued by the U.S. Department of Energy in May 2010 and the *Policy Framework for PACE Financing Programs* issued by the White House in October of 2009.

Four states, Maine, New Hampshire, Oklahoma, and Vermont, have passed legislation allowing PACE liens that are not required to take a first-lien position ahead of a mortgage loan. In addition, each of these programs include the DOE and White House safeguards. The programs incorporate some combination of underwriting and disclosures to ensure the home owner can afford the payments, the combined loan-to-value of the mortgage loan and the PACE lien does not exceed a certain percentage of the value of the home, the home improvements meet high-quality standards and the investment will “pay for itself” over the life of the assessment. Other consumer and lender protections also have been employed by these states and consequently mortgages with these PACE liens are allowable for purchase by Fannie Mae and Freddie Mac in these states.

NAHB recommends that FHFA review these subordinate-lien PACE programs as a possible way to structure energy efficiency financing programs to mitigate the risks of retrofit financing while simultaneously preserving the existing mortgagee's first lien status.

Conclusion

NAHB supports efforts to develop financing programs for energy efficient retrofits for residential and commercial properties. However, we are concerned that the first lien priority in most PACE programs will have a significant negative impact on the housing finance system and home owners. Thus, NAHB believes that FHFA's current restrictions and conditions on first lien PACE programs should be maintained.

NAHB recommends that FHFA and the Enterprises work with stakeholders in the housing and mortgage lending industries to resolve the impediments to the effective use of PACE programs as a means to finance energy retrofits in a manner that does not impair the functioning of the housing finance system. In this regard, NAHB encourages FHFA to review PACE programs structured as junior liens and that incorporate consumer disclosures and underwriting guidelines as a possible alternative in FHFA's prospective Environmental Impact Statement analysis.

Thank you for your consideration of NAHB's comments. If you have questions, please contact Becky Froass, Director, Financial Institutions and Capital Markets at 202.266.8529 or email at rfroass@nahb.org.

Sincerely,

David L. Ledford

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