CALIFORNIA ASSOCIATION OF REALTORS®

August 14, 2015

Edward L. Golding
Principal Deputy Assistant Secretary, Office of Housing
U.S. Department of Housing and Urban Development
451 7th Street S.W.
Washington, DC 20410

Re: FHA Single-Family Mortgages and Property Assessed Clean Energy Loans

Dear Deputy Assistant Secretary Golding:

On behalf of the 180,000 members of the California Association of REALTORS® (C.A.R.), I am writing in response to reports that the U.S. Department of Housing and Urban Development (HUD) is considering issuing a statement, guidance or pilot projects related to the Federal Housing Administration's (FHA) single-family mortgage program and Property Assessed Clean Energy (PACE) liens.

The use of PACE "super liens" has grown more in California than in any other state. It is likely thousands of existing FHA insured homes in California already have PACE "super liens" on title without HUD's or the FHA's knowledge. C.A.R. is concerned that HUD and the FHA attempts to regulate such loans may inadvertently disrupt California's real estate market. While C.A.R. and its members support the concept of PACE, C.A.R. respectfully requests that HUD and the FHA publicly adopt policy consistent with the Federal Housing Finance Agency's (FHFA) existing policy on PACE loans.

Specifically, this position would OPPOSE the use of PACE encumbrances with "super lien" priority that becomes senior to first-mortgage financing. Only by publicly objecting to the seniority or "super lien" status of PACE loans over FHA single-family mortgages will the FHA maintain consistency in the availability of mortgage financing for single family homes.

Additionally, C.A.R. is concerned that the manner in which PACE programs are being implemented in California puts consumers at risk. Namely, there are no standard truth in lending disclosures which threaten the safety and soundness of the FHA's Mutual Mortgage Insurance Fund (MMIF).

FHA Should NOT Accept PACE Liens as Senior to a First Mortgage

In order to ensure market stability, and to present a uniform policy for the secondary market, we request that HUD issue a statement directing their lenders and servicers that PACE liens may NOT be senior to any mortgage insured by the FHA. This would align the FHA's policy with the FHFA's policy. This consistency will avoid market confusion among home sellers, home buyers, lenders, servicers, and the real estate industry who have followed the FHFA guidelines for the last five-years.

The FHA, along with Fannie Mae and Freddie Mac (Enterprises) continues to make up the majority of mortgage financing for California's mortgage market. Therefore any policy change will have an immediate and broad impact on California's housing market. Currently, California's housing market continues to underperform with low sales and low first-time homebuyer participation. If the FHA allows PACE liens to be senior without objection then non-FHA borrowers (who make up the majority of homebuyers) will be discriminated against in purchases of properties with PACE liens; and transactions would become more complicated as servicers, title companies, escrow companies and other transaction participants struggle to implement competing PACE procedures. HUD must ensure FHA policy promotes and supports a healthy housing market and maintaining policy continuity with the FHFA on PACE liens is an important component to strengthening California's housing market.

Concerns with PACE Seniority Implementation

C.A.R. is concerned about a tacit approval by the FHA of PACE "super lien" priority and the affect it will have on existing subordinate liens, the home equity loan market and the accepted rule of determining lien priority/seniority based on time of recording. For example, if a buyer takes out an FHA mortgage to buy a $100,000 home, and five-years later takes out a home equity loan to remodel the kitchen the home equity loan is junior to the FHA mortgage. Suppose then, a year later the same owner agrees to a PACE lien to put solar panels on the home. The PACE lien will have the status of a tax lien and be senior to the earlier encumbrances. Even if the FHA does not object to PACE being senior, where does the second lien fall in lien priority if they do not agree to being subordinate to PACE? By allowing the PACE liens to jump not just the first mortgage in lien seniority, but existing subordinate liens as well, the home equity loan market will become higher risk and could dry up or become cost prohibitive. This confusion of lien seniority will also make distressed transactions such as REOs and short sales more difficult.

Taxpayer Protection

C.A.R. is also concerned about the impact PACE "super liens" will have on the safety and wellbeing of the mutual mortgage insurance fund (MMIF). PACE encumbrances may approach 10 percent or 15 percent of the value of a home. With a 3.5 percent downpayment it is very likely many FHA single family residences would immediately wind up with negative equity following a PACE lien. If a FHA buyer assumes a PACE loan will the FHA count the outstanding PACE lien as a loan against the equity in the home? If so, then FHA buyers may not qualify for many PACE homes because they could be upside down at purchase. If the FHA does not oppose the senior position of the PACE lien then the FHA could easily find there is not enough equity left in the property to fully cover its losses if the loan goes into default.

Pandora's Box

Absent legislation subordinating the specific tax assessment to a first-mortgage and existing liens on a property, which is not in place, the implementation of the PACE program is through tax assessments which take a senior position. C.A.R. is concerned that if the FHA does not object to PACE "super lien" priority then other interest groups will have their "pet projects" paid for through tax assessments. Statutory authority has already been expanded from solar, to energy conservation, to water conservation. In fact, C.A.R. is even now fighting California Senate Bill SB 602 (Monning). SB 602 would encourage homeowners to make earthquake retrofits to their properties and pay for it through a PACE-type loan that has a senior tax status on the property.

As other states adopt PACE-like programs, we can easily envision fire prevention improvements to homes, tornado retrofits, hurricane retrofits, home security system installations and many other pet projects of various interest groups. How many tax assessments is the FHA willing to allow to be in a senior position to a FHA first-mortgage? Under California's PACE program multiple projects may be funded with a single PACE "super lien." If the FHA limited the PACE "super lien" to specific improvements, would FHA's underwriters and servicers be willing to take the risk of ensuring the lien only covered the cost of installing the "approved" project?

PACE still has Many Flaws

C.A.R.'s members support the concept of PACE. It provides a voluntary market-based alternative to point-of-sale mandates to make homes more energy efficient. However, C.A.R. has had many concerns with the unregulated implementation of PACE lending in California and its negative impacts on homeowners and real estate transactions. Most alarming is that this unregulated lending is not subject to industry standards or "best practices." This in turn has led to:

- **<u>A lack of uniform disclosure of loan terms by PACE lenders.</u>** This lack of uniformity or standard disclosure makes it difficult for borrowers to shop and compare a PACE program's rates and costs to more conventional credit lines. It also makes it difficult to know the actual terms and conditions of the loan.

- **<u>Rates and fees that border on usury.</u>** It is important to remember that in California a PACE "super lien" is a <u>senior tax lien</u> serviced by the county tax collector. By any reasonable analysis they should have an interest rate at or even below a first mortgage; however, PACE interest rates reportedly range from six-percent to nine-percent. These rates exceed current home equity loans. PACE liens also carry high origination fees and some still have prepayment penalties. (See attached document)
- **<u>Contractors overcharging for service or recommending unnecessary equipment.</u>** Borrowers rarely shop contractors whose projects are funded by PACE because the contractors are themselves the arranger of credit and proactively going to the consumer and selling them the improvement.
- **<u>The borrower not being underwritten for the loan.</u>** Because the PACE lien is attached to the property, collected via the tax bills, and transfers with title for as long as the loan term, PACE programs underwrite the property and the equity in it, but <u>NOT</u> the actual borrower. It is up to the borrower to determine if they can afford the loan.

Problems with Closings

C.A.R. has recently heard from multiple agents and brokers that even when a PACE "super lien" is paid off as part of a real estate transaction, lenders are counting this as a "seller contribution" or "seller concession," making many loans unqualified. We request that HUD and the FHA direct its lenders and servicers NOT to treat the payoff of PACE "super liens" as a seller concession.

The California Association of REALTORS® seeks to be a resource to HUD and the FHA in the ongoing development of its policy on PACE liens and FHA's single-family mortgages. If we can be of any assistance, please do not hesitate to contact Matt Roberts, C.A.R.'s Federal Government Affairs Manager at (213) 739-8284 or matthewr@car.org. Thank you for your consideration of our concerns.

Sincerely,

Chris Kutzkey

Chris Kutzkey
2015 President, California Association of REALTORS®

cc: National Association of REALTORS®

Current PACE Program Offerings

	HERO Program	CaliforniaFirst	Ygrene	Figtree	mPower (Placer County Administered)	emPower (Administered by Credit Union for Counties of Santa Barbara, Ventura and San Luis Obispo)
Type	Lien	Lien	Lien	Commercial Lien	Lien	Unsecured Personal Loan
Prepayment	None	None	3% to 5% in the event of prepayment. At the start of loan, application can opt to increase interest rate by .49% and not be subject to penalty	Years 1-5: 5% Years 6-10: 3% Years 11-20: None	A prepayment premium will be charged if the assessment is repaid within the first 5 years. Graduated premium structure is as follows: 5% within the first year (95% of the additional payment goes toward the principal) , 4% within year 2, 3% within years 3 through 5	None
Interest Rates (5 year-20 year)	5.95%-8.95%	6.75%-8.75%	5.99%-8.25%	4.50%-6.99%	6%	3.9% and up (Was 5.9%) - Lower Rate Available Until Funds Exhausted
Origination Fee	6.95% of total loan amount plus additional administrative fees *	$519 plus additional administrative fees *	$884 plus additional administrative fees *	Up to 4% of the total financing	None plus additional administrative fees *	None

Annual Fees	$35 (adjusted for cost of living increases in subsequent years to maximum amount of $95)	$33	$63	$30 for every $1,000 of the annual assessment amount.	$25	None
Minimum Loan Amount	$5,000	$5,000	$5,000	$5,000	$2,500	$1,500 (Max Financed Loan Amount $30,000)
Total Upfront Costs	**See, origination fee + First calculated loan payment**	**$6,454,12 (Based on a $34,600 principal loan @25 years)**	**$4,425 (Based on a $35,000 principal loan @20 years)**	**$4,068.61 (Based on a $35,000 principal loan @ 20 years)**	**$3,818.49 (Based on a $35,000 principal loan @ 20 years)**	**First calculated loan payment**
*Note: Additional administrative fees cover a multitude of servicing functions and loan initiation (i.e. recording fees, title costs, bond counsel, tax administration, foreclosure reserve account, program fees, processing fees, permit fees, program sponsor, etc.)						
Note: Financed Loan Amount for PACE under CA law not to exceed 15% of the value of the property up to $700,000 and 10% or less of the remaining property value						