

August 16, 2016

The Honorable Julián Castro  
Secretary  
United States Department of  
Housing and Urban Development  
451 Seventh Street, SW  
Washington, DC 20410

The Honorable Robert A. McDonald  
Secretary  
United States Department of Veterans Affairs  
810 Vermont Avenue, NW  
Washington, DC 20420

Dear Secretaries Castro and McDonald,

The undersigned trade associations, representing the vast majority of mortgage lenders of all sizes and charter types and real estate professionals in the United States, are writing to express our concern over recent actions taken by the Department of Housing and Urban Development on behalf of the Federal Housing Administration, as well as by the Department of Veterans Affairs, with regard to Property Assessed Clean Energy (PACE) loans.

Prior FHA and VA policy barred the financing or refinancing of a home unless the property was free and clear of any liens other than the FHA-insured or VA-guaranteed mortgage. Because PACE obligations are collected through property tax payments, they exhibit a senior lien position to an FHA or VA loan. Thus, prior FHA and VA policy was designed to ensure that obligations like a PACE “super lien” would not erode the value of the collateral in the event of foreclosure or the sale of the property.

The guidance issued for the FHA and by the VA on July 19, 2016 now allows for the approval of mortgages for the purchase or refinance of properties with PACE obligations, provided they meet certain requirements. Among the requirements in the new guidance is the stipulation that the outstanding PACE loan obligation does not take first lien position ahead of the FHA-insured or VA-guaranteed mortgage. However, the guidance does provide that delinquent PACE loan amounts will retain a first lien position. Allowing any PACE loan amount to hold a senior priority undermines the lender’s (and the government’s) collateral position and disrupts the very nature of secured lending.

Moreover, rather than requiring definitive subordination of the PACE loan to the FHA or VA mortgage, the new guidance simply declares that a PACE loan structured as a tax assessment is not a super lien. But this declaration is a form over substance evasion that fails to protect the FHA Mutual Mortgage Insurance Fund and the VA loan guaranty program.

Furthermore, the July 19th guidance raises a host of serious consumer protection concerns. PACE loans are not typically accompanied by federal Consumer Financial Protection Bureau disclosures and protections associated with home mortgages, including the new Know Before You Owe disclosures, right of rescission protections, or the Ability to Repay standards. This is because PACE financing has been

conveniently classified as a tax assessment rather than a loan. However, a PACE loan is still a financial obligation that can negatively affect one's mortgage repayment ability. Borrowers may not fully understand the consequences of assuming an increased financial obligation on their tax bill. These borrowers also may not be able to effectively compare the cost of a PACE loan to that of more conventional financing—which typically is available at a significantly lower interest rate, with CFPB disclosures. Consequently, the existing PACE dynamics heighten the risk of borrower delinquency, which could lead both FHA and VA to incur higher defaults and loss severities than if PACE loans were required to be properly underwritten and subordinate to the first mortgage in the event of foreclosure.

It is important to note, although outstanding PACE loan obligations technically “run with property,” real estate professionals report that many subsequent purchasers of these homes reject the presence of a PACE payment obligation and insist that the seller extinguish the PACE financing before consummating the purchase. This leaves the original borrowers with a closing table surprise and far less in sale proceeds than they anticipated. The presence of the PACE obligation may also negatively impact home values, especially in foreclosure situations.

Our associations support responsible efforts to provide homeowners with affordable and accessible financing for energy efficient home improvements, and sounder alternatives to the FHA's and VA's new PACE guidelines already exist. We urge you to suspend the applicability of the proposed FHA and VA PACE guidelines and issue the proposal for notice and comment so that lenders, borrowers, home improvement providers, and others may be given the opportunity to comment and assist the Departments in establishing policies that better protect consumers, lenders, and taxpayers.

Sincerely,

American Bankers Association  
American Land Title Association  
Appraisal Institute  
Credit Union National Association  
Housing Policy Council of the Financial Services Roundtable  
Independent Community Bankers of America  
Mortgage Bankers Association  
National Association of Federal Credit Unions  
National Association of REALTORS®  
Real Estate Services Providers Council  
The Realty Alliance