TO: State and Territory Energy Offices
FROM: Sandy Fazeli, Senior Program Director, NASEO
RE: Residential Property Assessed Clean Energy Developments
DATE: August 3, 2016

On July 19, 2016, the White House announced the "Clean Energy Savings for All Americans" Initiative, a cross-agency federal government partnership to increase access to solar energy and promote energy efficiency across the United States and, in particular in low- and moderate-income communities. This initiative is underpinned by the Obama Administration's goal to deliver 1 gigawatt (GW) of solar to low- and moderate- income families by 2020.

The announcement includes several components:

- Efforts by the U.S. Department of Housing and Urban Development (HUD), U.S. Department of Veterans Affairs (VA), and the U.S. Department of Energy (DOE) to unlock Residential Property Assessed Clean Energy (R-PACE);
- DOE's Community Solar Challenge to help communities increase solar deployment;
- Technical assistance provided to Low Income Housing Energy Assistance Program (LIHEAP) grantees on using LIHEAP funding for low cost energy efficiency and renewable energy;
- The launch of the Solar Training Network; and
- Dialogues to finance and overcome barriers to creating healthier communities, among many federal, state, local, and business announcements.

The question and answer (Q&A) below focuses specifically on the efforts by various federal agencies to unlock single family homeowners' access to R-PACE (as this has been a primary area of focus for members of NASEO's Financing Committee); however, we will keep our members up-to-date on new details covering the whole announcement as we learn more.

What does the R-PACE guidance from HUD and VA say?

HUD's Federal Housing Administration (FHA) released Mortgagee Letter 2016-11 on July 19, 2016, a move that was originally signaled in August 2015 when FHA announced its intent to release guidelines for the use of FHA financing on properties with PACE assessments. Mortgage Letter 2016-11 includes several key positions and guidelines and indicates that a home with an existing R-PACE obligation is eligible for FHA-insured mortgage financing provided that the mortgage lender determines that the following conditions have been fulfilled:

- The PACE obligation is collected and secured in the same way as a special assessment;
- The property becomes subject to a senior-lien (superior to the FHA-insured mortgage for delinquent regularly scheduled PACE obligation payments, not for the full outstanding PACE obligation.
- The existence, amount, and expiration of the PACE obligation must be readily apparent to mortgagees, appraisers, borrowers, and other parties to an FHA-insured mortgage transaction in the public records. During the sale, the property sales contract must indicate whether the obligation will remain with the property or be paid off by the seller at or prior to closing. Where the PACE obligation remains outstanding, the appraiser must analyze and report the impact to the value of the property. Additionally, the terms and conditions of the PACE obligation must be fully disclosed to the borrower and in the sales contract.
- The PACE obligation stays with the property, and the responsibility for paying the assessment will be transferred from one property owner to the next even through a foreclosure sale.

The VA's Veterans Benefits Administration released Circular 26-16-18 on July 19, 2016 to address origination and loan processing requirements for VA-guaranteed loans when a property is subject to PACE obligations. Similar to FHA-insured properties, homes with an existing PACE obligation are eligible for VA-guaranteed financing provided the following requirements are met:

- The PACE obligation is collected and secured in the same manner as a special assessment;
- The property may be subject to a lien that is superior to the VA-guaranteed loan for delinquent payments; however, it must not be subject to a lien superior to the mortgage for the full PACE obligation amount;
- The existence of and information on the PACE obligation are readily apparent to mortgagees, appraisers, borrowers, and other parties to a VA-guaranteed loan transaction.
- The sales contract must indicate whether the PACE obligation will remain with the property or be satisfied by the seller, and all terms and conditions must be fully disclosed to the borrower.
- The appraiser must analyze and report the impact of the PACE improvements and the obligation on the value of the property;
- If the lender requires a borrower to escrow funds to ensure the PACE obligation is paid, it must open and manage the account(s) consistently with federal, state and local law.

In other words: for both FHA-insured and VA-backed mortgages in a foreclosure sale, the property may only become subject to a lien that is superior to the federally-backed mortgage for the delinquent amount owed, may not be subject to a superior lien for the full outstanding PACE obligation at any time, and there can be no acceleration of the remaining future installments that would have been due. In the event of a sale, including a foreclosure sale, the future installments/assessments may continue with the property, with the new homeowner to take on responsibility for these installments under the PACE obligation, unless they are satisfied prior to the sale.

What portion of the market will this affect?

Even though FHA and VA have an important market presence, their financing does not represent the entirety, nor a majority, of the U.S. single family home market. According to Renovate America, in 2015 FHA products represented 17.9 percent of overall mortgages with 21.9 percent of mortgage originations at purchase and 13.1 percent at refinancing.

The government-sponsored enterprises (GSEs), Fannie Mae and Freddie Mac, represent a much larger market share; however, the guidance from FHA and VA does not affect these two bodies as they have been placed into conservatorship run by the Federal Housing Finance Administration (FHFA), which opposes the senior-lien position of PACE obligations.

Can we expect this announcement to have an impact on the GSEs?

The Clean Energy Savings for All Initiative does not include FHFA, and thus does not provide guidance on the ability of properties with PACE liens to access Fannie Mae or Freddie Mac financing – the majority of the residential mortgage market. The FHFA has maintained its position against the senior-lien position of PACE obligations and has instructed the GSEs not to purchase or guarantee mortgages for homes participating in R-PACE programs. Until this position changes, the majority of the mortgage market will not be readily accessible to properties with existing R-PACE liens.

FHA representatives have indicated their willingness to educate FHFA on their experience handling mortgage transactions involving PACE obligations, as well as share data related to the performance and value of properties with R-PACE liens.

What does DOE's best practices guidance on R-PACE say?

According to DOE:

> The revised Best Practice Guidelines for Residential PACE Financing Programs focus on best practices for program design, including protections to both consumers who voluntarily opt into PACE programs, and to lenders who hold mortgages on properties with PACE assessments; compatibility of PACE with other energy efficiency programs and services; and evaluation of program outcomes, including cost effectiveness, energy savings, and non-energy benefits such as improved health and comfort. The guidelines can also be used by PACE program administrators, contractors and consumers to plan, develop, and implement programs and improvements that effectively deliver home energy upgrades. DOE developed these revisions to the original "Guidelines for Pilot PACE Financing Programs," initially issued on May 7, 2010, to reflect the evolving structure of the PACE market, and to incorporate lessons learned from various PACE programs that have been successfully implemented since the original guidelines were issued.

DOE is seeking input on the draft document now through August 19, 2016. More information on submitting comments is available at http://energy.gov/eere/slsc/downloads/best-practice-guidelines-residential-pace-financing-programs. **NASEO is seeking State Energy Office feedback on these guidelines as well as your interest in having NASEO develop a set of comments on the states' behalf.**

How will NASEO be keeping State Energy Offices up to date on more R-PACE developments?

NASEO will host a conference call on **Monday, August 8 at 2:00 to 3:00 pm Eastern Time to review the announcement, with a particular focus on the R-PACE updates, their impact on states' R-PACE efforts, and ways NASEO, DOE, and other organizations can provide support and assistance to your offices.** During this call we hope to gauge State Energy Offices' interest in participating in an R-PACE Taskforce that NASEO will organize and convene, as well as in preparing a set of comments on DOE's revised best practices guidelines.

In addition to the R-PACE Taskforce, NASEO will share updates on R-PACE and other relevant financing initiatives through the Financing Committee's bi-monthly calls and online email listserv and forum. To learn about the online forum or to discuss NASEO's next steps in further detail, please contact Sandy Fazeli at sfazeli@naseo.org.