



July 9, 2010

The Honorable Shaun Donovan
Secretary
Department of Housing and Urban Development
451 7th Street, SW
Washington, DC 20410

The Honorable Steven Chu
Secretary
Department of Energy
1000 Independence Avenue, SW
Washington, DC 20585

Dear Secretaries Donovan and Chu:

Many homeowners today are concerned about high energy costs and excessive energy consumption. However, making the structural changes to a home in order to reduce energy consumption and costs requires a significant upfront investment. This is why many policymakers have supported the Property Assessed Clean Energy (PACE) loan program, which allows consumers to finance the improvements through a loan made by a municipality, which is repaid through their properties' tax assessment. The Mortgage Bankers Association (MBA) has concerns about the PACE program and believes there are better ways to finance home energy improvements.

While MBA supports energy efficiency in homes and consumers' access to financing for energy efficient improvements, PACE loans present a number of obstacles to responsible mortgage lending. MBA appreciates the guidance¹ issued by the Department of Energy (DOE) on PACE loans, such as requiring quality controls over the municipalities of the programs, yet many significant concerns remain.

First and foremost, because the PACE loan is added to the property's tax assessment, the debt is ahead of any other lien on a property, including a mortgage. As a result, Fannie Mae and Freddie Mac (currently the largest sources of mortgage liquidity) recently announced that they will not purchase mortgages secured by properties associated with PACE loan. Furthermore, the Federal Housing Finance Agency (FHFA), Fannie Mae and Freddie Mac's regulator, also has publically expressed concern about the safety and soundness challenges posed by PACE loans and just this week directed Fannie Mae, Freddie Mac and the Federal Home Loan Banks to take action to protect the safety and soundness of their operations. The Federal Deposit Insurance Corporation (FDIC) issued a Financial Institution Letter shortly thereafter referencing FHFA's guidance and that insured institutions may have difficulty selling residential mortgages to Fannie Mae and Freddie Mac.² Earlier, the *Wall Street Journal*, on May 17, 2010, reported that such announcements have effectively shut down the local PACE programs.

¹ Guidelines for Pilot PACE Financing Programs, Department of Energy, May 7, 2010.

² Alert on FHFA Statement Relative to Concerns with Certain Energy Lending Programs, Federal Housing Finance Agency, Financial Institution Letter 37-2010, July 6, 2010.

In addition, MBA is concerned that PACE loans may limit a consumer's financial choices. The absence of proper underwriting and approval processes associated with PACE loans may cause homeowners to take on too much debt and impede their ability to meet their existing debt obligations, refinance into a new loan, or obtain a mortgage modification, if necessary, because of the additional debt. The PACE debt could also increase the borrower's risk of defaulting on their mortgage and put them at risk of foreclosure. Also, selling a property with an outstanding PACE loan balance on the tax assessment may be less appealing to some homebuyers, thus precluding resale opportunities.

In order to prevent these concerns from forestalling the benefits of an environmentally favorable and sustainable home and lifestyle, MBA believes that the PACE program must conform, at a minimum, to the following recommendations:

- **PACE Loans Must Not Be Superior to Existing Mortgage Liens** – The Department of Housing and Urban Development (HUD), the DOE, and/or state and local governments as appropriate should require municipalities receiving federal funding that make such loans to notify the lienholder or lienholders and obtain their permission prior to a PACE loan being made and added to the property tax assessment. Furthermore, an agreement should be required, or a mechanism put into place, that assures the lender that, in the event of a default and foreclosure, the mortgage lender would only be required to pay the annual tax assessment, minus the PACE loan portion, and the agreement must provide that the PACE loan is subordinate to the existing mortgage debt. In the instance where the municipality requires that the full outstanding balance of the tax assessment (greater than one year's assessment), is due upon foreclosure, the municipality must be required to subordinate the PACE portion of the tax assessment to the existing mortgage debt.
- **Establish Minimum Standards for Home Energy Improvements** – HUD, DOE, and state and local governments as appropriate should establish minimum standards for contractors to meet in performing home energy improvements in association with the PACE programs. Federal regulators should also set minimum standards for the estimated monthly cost savings from the energy efficient improvements and prohibit government funding if the monthly payment does not match the savings, within a reasonable tolerance. Furthermore, municipalities making PACE loans should be required to perform inspections of all work completed; inspections would ensure the quality and completion of the work and would serve as reference material in judging whether the contractors should continue serving in association with the PACE program.
- **Ensure Program Accountability** – HUD, DOE and state and local governments as appropriate should ensure program quality by random or regular reviews or audits of the municipalities making PACE loans. Poorly managed programs should be suspended from making PACE loans for an appropriate period of time.

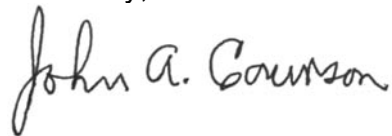
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The changes to the PACE program described in the first recommendation would significantly alter the program. It would likely require the PACE loan to be recorded as a lien separate from the tax assessment. However, MBA recognizes that such changes may be difficult to achieve. For this reason, MBA would like to point out that there are established mortgage products that would achieve the financing consumers are seeking to make energy-saving improvements, such as energy efficient mortgages (EEMs) and home improvement loans. The Federal Housing Administration (FHA) offers both products and has been tested in the marketplace over many years. These programs, and others, are viable alternative to PACE loans, if the program is left without a remedy.

We would like to meet with you to discuss these concerns and solutions. Please contact Andrew Szalay, at (202) 557-2941 or aszalay@mortgagebankers.org. We appreciate your time and look forward to hearing from you.

Sincerely,

A handwritten signature in black ink that reads "John A. Courson". The signature is written in a cursive, flowing style.

John A. Courson
President and Chief Executive Officer

CC: The Honorable David Stevens, Federal Housing Commissioner
Mr. Edward DeMarco, Acting Director, Federal Housing Finance Agency