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March 26, 2012

Mr. Alfred M. Pollard
General Counsel
Federal Housing Finance Agency
Eighth Floor, 400 Seventh Street SW
Washington, DC 20024

Re: RIN 2590-AA53; Mortgage Assets Affected by PACE Programs

Dear Mr. Pollard:

On behalf of the over one million members of the National Association of REALTORS® (NAR), I am writing in response to the Federal Housing Finance Agency's (FHFA) recent Advanced Notice of Proposed Rulemaking, published at 77 Fed. Reg. 17, (January 26, 2012) (the "ANPR"), Mortgage Assets Affected by PACE Programs. These members are involved in all aspects of the real estate industry, including buying, selling and managing commercial and residential real property. Our members have an interest in Property Assessed Clean Energy (PACE) programs because of the implications these programs may have for broader real estate financing issues.

NAR is not opposed to the concept of PACE loans. On the contrary, NAR is strongly supportive of incentive-based financing programs that enable homeowners to improve the energy efficiency of homes and take advantage of the reduction in their energy costs.

Background

PACE programs provide a means of financing certain kinds of home improvement projects. Specifically, PACE programs permit local governments to provide financing to property owners for the purchase of energy-related home-improvement projects, such as solar panels, insulation or energy efficient windows. Homeowners repay the amount borrowed, with interest, over a period of years through an assessment added to their property tax bill.

Over the last three years, more than 25 states have authorized local governments to establish PACE-type programs. In most, but not all, states that have implemented PACE programs, the liens that have resulted from PACE program loans have priority over mortgages, including pre-existing first mortgages. In the case of a mortgagee foreclosing on a property, the PACE loan must be paid off before any other financial obligation running with the property, including first mortgages.

The FHFA began reviewing these programs in 2009. On July 6, 2010, the FHFA issued a statement that, in part, states:

"The Federal Housing Finance Agency has determined that certain energy retrofit lending programs present significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac and the Federal Home Loan Banks….First liens established by PACE loans are unlike routine tax assessments and pose unusual and difficult risk management challenges for lenders, servicers and mortgage securities investors….They present significant risk to lenders and secondary market entities, may alter valuations for mortgaged-backed securities and are not essential for successful programs to spur energy conservation."

This statement had the result of chilling any further demand for these programs.

EQUAL HOUSING OPPORTUNITY

General Comments to Issues Raised in the ANPR Related to Real Estate

PACE is an innovative approach that helps to resolve on the major obstacles to market-wide spread of energy efficiency improvements – i.e., the split-incentives market failure: Owners opt not to invest because they are afraid they won't be able to recoup the full investment if they are planning to sell the property. By having access to financing that conveys with the sale of the property, there is a potential to improve the energy efficiency of homes.

These comments do not respond to every question that is included in the ANPR; rather, NAR is commenting generally on those elements of PACE programs which have direct relevance to Realtors and their interests.

NAR has identified the following areas that will need to be addressed for PACE programs to succeed:

<u>Credit and Mortgage Availability</u>
NAR is concerned that PACE loans could have an adverse impact on credit and mortgage availability. Like property taxes, PACE liens take priority over mortgages. That makes the bonds easier for municipalities to sell. But if a home is foreclosed on, the liens are paid before the mortgage lender can recoup any money. The presence or potential presence of a PACE loan, taking the first position ahead of the mortgage, invariably leads to the devaluation of the mortgage as a secured asset. This has the effect of either making mortgages more risky and costly or leading to situations where mortgage credit is tighter or unavailable. Furthermore, it is unclear at best whether the resulting improvements add enough value to compensate for the additional risks.

<u>Secondary Mortgage Market Liquidity and Risks to Broader Financial Markets</u>
While the first lien position offered in most PACE programs minimizes credit risk for investors funding the programs, it alters traditional lending priorities. Underwriting for PACE programs results in collateral-based lending rather than lending based upon ability-to-pay, the absence of Truth-in-Lending Act and other consumer protections, and uncertainty as to whether the home improvements actually produce meaningful reductions in energy consumption. Similar to the points made above, the additional risk and uncertainty associated with having a PACE loan attached to a property and in the first lien position, will invariably lead to increased risk assessment among investors in mortgage backed securities and mortgage loans.

<u>Disclosure Concerns</u>
Realtors are very concerned about issues they are required to disclose about a property. Depending on state law, Realtors are required to disclose anything that could impact the value of a property, from inclusion in a floodplain to the location of a solid waste transfer facility. The more items that are required to be disclosed, the more liability is increased if the Realtor does not include an item. Other state laws are more ambiguous and direct Realtors to disclose anything that may materially impact the value of a property. With regard to PACE loan liens, NAR recommends that the FHFA conduct additional legal research into whether or not PACE liens and special tax assessments fall into the category of items related to the property that should be disclosed. There are limits to disclosure and PACE loan liens fall into a gray area which would benefit from further exploration.

<u>Concerns Related to the Completion of the Transaction</u>
Because these PACE loans run with the property and not with the property owner, the information on the tax assessment about the loan will need to be explained for each new buyer. If we assume that the average home is sold every five years, and the average length of the PACE loan is 20 years, then the Realtor will be responsible for explaining this special tax assessment an average of four times over the life of the loan.

Once the prospective buyer learns about this new cost to purchasing the home, this information may cause delays in the completion of the transaction or even a cancellation. The prospective buyer may ask questions about the special assessment, or may question the value of the home improvement financed by the PACE loan, which could have been done ten years prior. The energy efficiency and renewable energy investments are designed to "pay for themselves," which is to say that the homeowner's utility bill goes down by more than their property tax bill goes up. However, it is difficult to measure the benefits of these improvements, because the way an owner uses energy in a home may change over time, depending on variables such as weather and family composition and whether or not the energy efficiency retrofit has become technologically outdated, or was ever as efficient as it was supposed to be.

Appraisals
Many markets are still determining what, if any, value green features add to real property. As such, Appraisers are facing the challenge of determining value in what is largely a developing aspect of valuation. Education opportunities for appraisers in this area are just now becoming widely available. The Appraisal Foundation is responsible for establishing standards and qualifications for appraisers. The Foundation recently announced a call for subject matter experts to help their Appraisal Practices Board develop voluntary guidance that will not be available for many months.

Refinancing Concerns
For a property under a PACE lien, refinancing could be problematic as well. All of the issues related to lien-priming aspects of PACE loans would also be apparent when the current owner goes to a lender to refinance the property. Homeowners who participate in the PACE program with the goal of reducing their monthly expenses through lower energy bills could find themselves unable to take advantage of the significant savings that even a single percentage drop in interest rates can bring with it.

Conclusion

The NAR appreciates the opportunity to comment on the PACE loan programs and supports providing property owners with the education, incentives and resources they need to improve their homes and save energy.

NAR also appreciates the emphasis on the voluntary nature of these programs, but believes that, at this time, the safety and soundness of real estate mortgage markets must take precedence over other ancillary, albeit important, concerns.

Sincerely,

Maurice “Moe” Veissi
2012 President, National Association of REALTORS®