CLEAN ENERGY

Keeping PACE

Increasing consumer protections is strengthening a clean energy financing program for homeowners.

BY JOCELYN DURKAY

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California is the founder of PACE and my own hometown, Berkeley, was where it was initiated," says Senator Nancy Skinner (D), referring to the Property Assessed Clean Energy financing program, launched in 2008, which allows homeowners to pay for energy efficiency, renewable energy or water conservation improvements through an assessment on their property taxes.

Senator Nancy Skinner California

California has the largest residential PACE, or R-PACE, market. "We've already empowered more than 150,000 homeowners in California," she says, "which we're very proud of." But, like most new programs, "Once it's out in the field, you learn where it needs improvements." So, after hearing consumer complaints about some abuses in the program, California lawmakers recently made some changes.

How It Works

Homeowners who want to make certain improvements—switching to an energy-saving heating or cooling system, adding solar panels to the roof or increasing the home's resistance to storms or earthquakes—but who don't have the savings to pay for them all at once, can sign a PACE contract. With funding from the private sector, PACE requires no down payment and pays the contractor in full when the work is completed. The customers then repay a PACE administrator slowly, over time, through an assessment (or lien) on their property that is added to their tax bill.

PACE programs are private-public partnerships: State legislatures must enact enabling legislation, localities may choose whether to opt in (requiring them to collect payments), and private-sector administrators finance and manage the programs.

Residential PACE was a $2 billion investment in 2016. In a study that year of California's R-PACE program, the average assessment in the state was slightly more than $20,000—a sizable improvement project for many homeowners.

According to publicly reported California data, the most common R-PACE assessment has a 20-year contract length with an average principal of $28,233, resulting in an average annual payment of $2,720. Several concerns have made their way to the California Legislature, however, since the program began almost a decade ago: deceptive contractors, unclear repayment terms, customers' lack of understanding about PACE's structure and customers defaulting on their assessments. Even though the reports represented a small percentage of the projects, lawmakers took them seriously—and responded.

Protecting Consumers

Last year, California became the first state to adopt comprehensive consumer protection legislation for R-PACE homeowners under a bill sponsored by Assemblyman Matthew Dababneh (D). It mandates new disclosure requirements modeled after federal "Know Before You Owe" mortgage disclosure practices, including giving customers three days to cancel from the time they sign a PACE contract. It also limits the methods and data contractors that program administrators can use to claim that an assessment will increase a property's market value.

Assemblyman Matthew Dababneh California

In October, California Governor Jerry Brown (D) signed two PACE-related bills into law. One strengthens disclosure requirements by adding a recorded oral confirmation, extends the three-day cancellation period to all contractors (not just to PACE contracts) and prohibits kickbacks to contractors for PACE referrals. In addition, program administrators must report twice a year on projects—including customers' missed payments and defaults.

The second bill introduces the first state regulatory structure and ability-to-pay requirements in the country and provides an enforcement mechanism to guarantee consumer protections.

"When I started reading reports of homeowner concerns, I wanted to make sure the Legislature effectively addressed the issue, ensuring that homeowners would be protected and putting to rest any concerns that discouraged people from participating in this program," Dababneh, chair of the Committee on Banking and Finance, says.

"California has engaged stakeholders who do not always see eye to eye, but all parties have come together to make consumer protection improvements in the PACE market a priority," he says. "Local governments, PACE program administrators, environmental groups, banks, credit unions and real estate interests have all come to meet with me to discuss how we can protect homeowners."

Overcoming Federal Lean on Liens

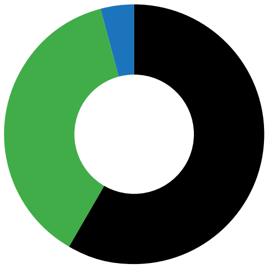
Residential PACE programs encountered a significant federal obstacle shortly after they began in 2008. The Federal Housing Finance Agency advised mortgage lenders in 2010 that it would not purchase or guarantee mortgages on properties with existing PACE liens, creating a de facto requirement that any assessment be paid off before a sale. The decision threw a wrench into many state efforts, suspending or terminating several R-PACE programs.

Today, only California, Florida and Missouri have active residential programs, although 22 states have passed enabling legislation. The picture for commercial PACE programs is quite different: 19 states and the District of Columbia have active programs, according to the advocacy group PACENation.

Florida and Missouri also have adopted consumer protections in statute. Florida, like California, has limited the size of a PACE lien to a percentage of a property's value and requires specific disclosure statements. Missouri legislators included protections to ensure homeowners pay only for the costs listed in the PACE contract. State law also requires that final costs be verified and that reports on assessments be prepared annually.

Federal entities and industry also are acting to protect consumers. In February, a network of PACE administrators and stakeholders adopted industry standards on consumer protections. The U.S. Department of Energy's best-practice guidelines for R-PACE, released last year, contained extensive protection recommendations. The Federal Housing Administration and the Veterans' Administration adopted their own PACE guidelines. And this spring, federal legislation was introduced in Congress to regulate the PACE industry.

WHAT PACE PAYS FOR



Energy efficiency upgrades: 58%
Renewable energy installations: 37%
Water efficiency upgrades: 4%

Source: PACENation, 2016

Not Waiting on the Feds

Some states, however, are not relying on federal entities to move ahead. "I think we

WHICH PROJECTS QUALIFY

As designated in statute, the following technologies are eligible for PACE financing in the three states with active residential programs:

California

- electric vehicle charging infrastructure
- energy efficiency
- renewable energy
- seismic strengthening
- water efficiency

Florida

- electric vehicle charging equipment
- energy conservation and efficiency
- renewable energy
- wind resistance

Missouri

- energy efficiency
- renewable energy

Sources: California Constitution, Florida Statutes and Missouri Revised Statutes

Senator
Eric Pratt
Minnesota

states can do a fair job without federal intervention," says Minnesota Senator Eric Pratt (R).

Several states with robust commercial programs have shifted their focus to developing options for homeowners. Minnesota, for example, has statutory language authorizing both residential and commercial PACE programs, but only commercial programs are operating there now. As plans developed for a new residential program, Pratt was aware of consumer protection concerns in other states. "All that troubled me and is why I wanted to get a task force together," he says.

He served as the lead in preparing the legislation, which passed this year, creating a 16-member Residential PACE Consumer Protection Legislation Task Force in the state Commerce Department. The task force will develop recommendations to address several consumer protection concerns, including the transfers of homes with PACE liens, customers' ability to repay and special considerations for low-income, elderly or vulnerable homeowners. All recommendations and suggested legislation for the residential program must be detailed in a report due Jan. 15, 2018, to the chairs and ranking minority members of the Legislature's Energy and Consumer Protection committees.

"I think my role as a legislator is to make sure that our state laws are a good balance between economic growth and consumer protection," Pratt says. He sits on both committees.

Pratt's bill suspended R-PACE activity until additional consumer protection legislation is enacted. "My hope is that Minnesota comes out with a program that can be a model for other states to follow," he says.

The Road Ahead

The last decade has proved that the design of state legislation significantly influences the success of residential PACE projects. Common components of effective legislation include a list of eligible improvements, cost-effectiveness requirements, guidance on transferring projects in a sale and mortgage-holder notification.

During foreclosure, any overdue portion of a PACE assessment must be paid first, as with all municipal assessments. Legislation can address concerns with this process by modifying that rule, which is called "limited subordination," or by clarifying that a new owner is not responsible for overdue balances and assumes the remaining lien balance, called "non-acceleration."

An emerging concern is whether the addition of a PACE lien increases the likelihood a homeowner will miss a payment or default altogether. Although a February report from the Kroll Bond Rating Agency stated that delinquency rates were below 2 percent for homes with PACE liens, the California Association of County Treasurers and Tax Collectors found that R-PACE default rates had increased in the last year. The data are incomplete, making it impossible to compare default rates of PACE users with those of homeowners statewide. California enacted legislation this session that will better capture the data needed to make this assessment.

Residential PACE financing is a growing opportunity, and legislatures are active in discussions about these innovative programs. Both Dababneh and Skinner say they'll continue to monitor PACE as it develops in California and respond to future concerns.

As Dababneh says, "Strengthening consumer protections through legislation is a win-win situation for everyone."