

# PACE, The New Subprime Market



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# Agenda



1. INTRODUCTION TO PACE
2. EXAMPLE CLIENT STORIES
3. PROBLEMS WITH PACE
4. LEGISLATIVE ADVOCACY
5. LITIGATION STRATEGIES
6. TAKING ACTION

# What is PACE?



- Property Assessed Clean Energy loans are used to finance home improvements that increase a home's energy efficiency.
- Approval based on equity. Minimal underwriting.
- Recorded as a voluntary tax lien, and collected through property taxes.
- Have superpriority status, bumping existing liens out of position.
  - Causes problems upon sale, refinance or modification.

A close-up photograph of a light-colored dog, possibly a Weimaraner, looking out of the open rear window of a car. The dog's head is resting on the window frame, and its gaze is directed towards the right side of the frame. The background shows a blurred outdoor scene with trees and a road.

# Home improvement financing that is simple and stress free.

That's our favorite part.

[GET STARTED](#)

## No Money Down. 100% Financing.

### Home Improvement Financing For Energy Efficiency Upgrades

Improve your family's comfort, health and safety, and you may save big on your monthly energy bills and boost the value of your most important investment. Enjoy no payments for up to 17 months\*

\*Based on date of funding; subject to underwriting guidelines and approval.

AGENCY	AGENCY PHONE NO.	RATE	AMOUNT
GENERAL TAX LEVY ALL AGENCIES		1.000000 \$	2,252.74
VOTED INDEBTEDNESS			
CITY-L.A. SANTA		.021297 \$	47.98
METRO WATER DIST		.003500	7.88
COMMNTY COLLEGE		.035956	81.00
UNIFIED SCHOOLS		.131096	295.32
DIRECT ASSESSMENTS			
FLOOD CONTROL	(626) 458-5165	\$	37.96
LACO VECTR CNTRL	(800) 273-5167		8.97
CITY LT MAINT	(213) 847-1363		42.45
COUNTY PARK DIST	(213) 738-2983		12.86
LA HERO	(800) 969-4382		6,994.64
CAFIRST	(949) 955-1500		5,295.85
LACITY PARK DIST	(213) 847-4722		33.96
TRAUMA/EMERG SRV	(866) 587-2862		69.53
LA STORMWATER	(213) 485-7422		30.26

Before: \$2,920.81

After: \$15,211.30 (over 40% of the household's gross income)

# Authorizing PACE



- A state adopts enabling legislation.
  - May also be used for other “public purpose” improvements, such as water efficiency, earthquake retrofitting and hurricane hardening.
- A local government (city, county or joint powers authority) contracts with a PACE “Administrator.”
- The PACE Administrator, which is a private company, can then originate PACE loans in that jurisdiction, usually using home improvement salespersons as loan brokers.

# PACE Administrators



# Rapid Growth



- Since 2008, more than 132,000 loans have been made totaling approximately \$3.3 billion, with \$2.85 billion originated in the last two years.
- PACE industry forecasts that the current \$3.3 billion in PACE financing will double within the next year, making it **fastest-growing form of financing** in the nation.
- Residential PACE enabling statutes have been enacted in twenty-five states.
  - California, Florida, Missouri, Vermont, and Maine have active residential PACE programs.



# These Are High-Cost Loans



- Interest rates average from 6 to 9%, with APRs over 10%.
- PACE borrowers pay points and fees of at least 5%, an annual administrative fee of about \$35 each year for the life of the loan, and steep pre-payment penalties.
- Almost anyone who can afford credit can get better terms elsewhere.
  - Only helpful to persons with poor credit and just the right amount of income.

# Example



- Ms. C. got a \$39,676 PACE loan for solar panels
  - 8.95 % rate, APR of 10.32 %
  - Total of payments on 20-year loan is \$84,393
  - Annual assessment is \$4,219.66
  - Her mortgage payment after escrow adjustment increased from \$990 to \$1,500 per month

# The Finance Side



- PACE is a goldmine:
  - Inflated prices
  - Minimal underwriting costs
  - Minimal servicing costs, no loss mitigation
  - **ZERO RISK** because of superpriority status
  - Yet interest rates are twice that of conventional for-profit lenders
- Financed through public bonds, which are then securitized.

# Collection



- Biggest threats:
  - Reverse mortgages
  - Impounded taxes
- Bond-holder can foreclose
- Tax lien sale
  - Steep penalties for delinquent taxes apply.
  - Usually takes several years to foreclose.
  - California's reserve fund protects pre-existing lienholders, *not* the homeowner.



# Client Stories

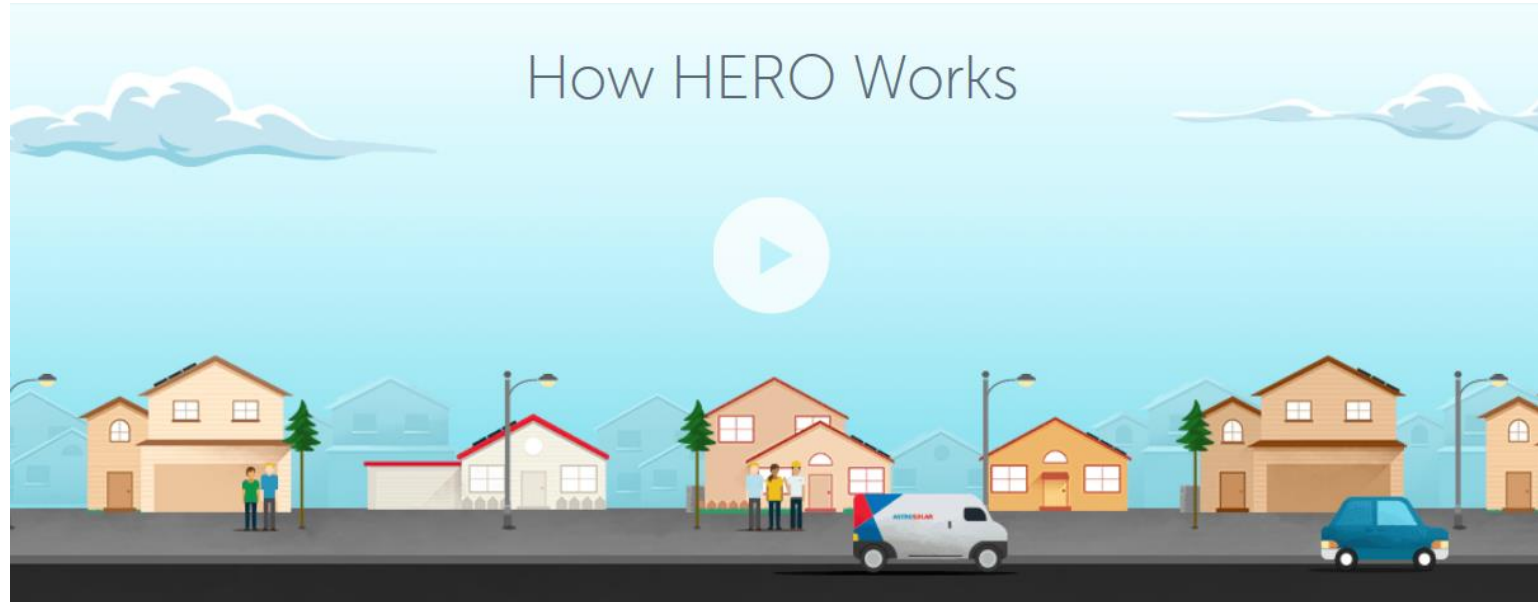
- Two PACE liens for the exact same work (which is not done).
- Telling a senior with dementia that her home would be red-tagged.
- Signing the contract and the completion certificate the same day.
- Offering non-efficient improvements to coerce homeowners to sign-up, but only billing PACE admin for authorized items.
- Claiming that energy bills will not only be eliminated, but DWP will pay the homeowner for extra energy generated.

# “It’s a Free Government Program”



- There *are* free government programs, and low-income homeowners often know that.
- Even where there is no direct misrepresentation, the government affiliation inspires trust, including as to pricing.
  - Participating in a program is different from negotiating a contract.
- Other key misrepresentations:
  - Rebates
  - Tax benefits
  - Energy savings

# “Affordable” Government “Partnerships”



By partnering with local governments, we've made energy and water efficiency upgrades more affordable for homeowners like you.

Up to 25-year terms • Borrow up to 15% of home's value • Competitive, fixed rates

SEE HOW MUCH YOU QUALIFY FOR

# Not Helping the Environment



- Contractors do not perform energy audits.
- Homeowners' energy usage does not decrease.
  - Most projects have no benefit
  - Partial exception for solar panels
  - No projects pay for themselves, as recommended by the Department of Energy.
- Contractors perform non-qualifying work.



# Contractors as Loan Brokers



- Do *they* even understand how PACE works?
- Door-to-door solicitation
  - “I’m here to talk to you about a County program,”
  - Not “I’m here from ABC Contractors ... do you need financing”
- Robo-calls
  - “We’ll do an *assessment* on your house to see what your house needs”
  - “The City wants to reward you for paying you property taxes”
  - They refuse to give a business name, and hang up.

# Brokering E-Contracts



- The finance application and assessment contract are presented on a tablet.
- There may be a phone call to verify basic terms.
- Contractors set up email accounts for seniors. The senior may not know how to access it, but the contractor does.
- Paper copies are rarely sent (even if there is no email listed on the contract).

# Prices Are Out of Control



cool life paint 2800 sqft \$23,150..  
17 windows ply gem \$23,000..

Special Instructions: Lifetime warranty on all wood and stucco apply  
contingent on all wood and stucco warranty is transferable  
to next home owner of property all stucco and wood  
flashing all fresh related to job protect  
install gutter around house were needed  
Work Excluded From This Contract: Reduce both security doors and front wood door

## Terms and Conditions:

- A. Approval and Acceptance: Owner/Buyer understands that this document is an offer to contract for the services of Contractor and is not binding upon Contractor until accepted by the corporate office of Contractors. Once accepted by contractor in writing or by commencement of work, this document shall become a valid and binding contract.
- B. Cancellation Fee: A Cancellation Fee of fifty percent (50%) of total contract price will be charged for cancellation after expiration of the three day period as set forth in the notice of Cancellation.
- C. Product Specifics: All Contractors' lifetime warranties are in addition to the manufacturer warranty but are subject to the assumption of responsibility of the manufacturer under its warranty.
- D. If commencement date of project is delayed due to customer, the progress payment is payable and due 30 days after contract date.

Payment Total Contract price to be: \$ 27650

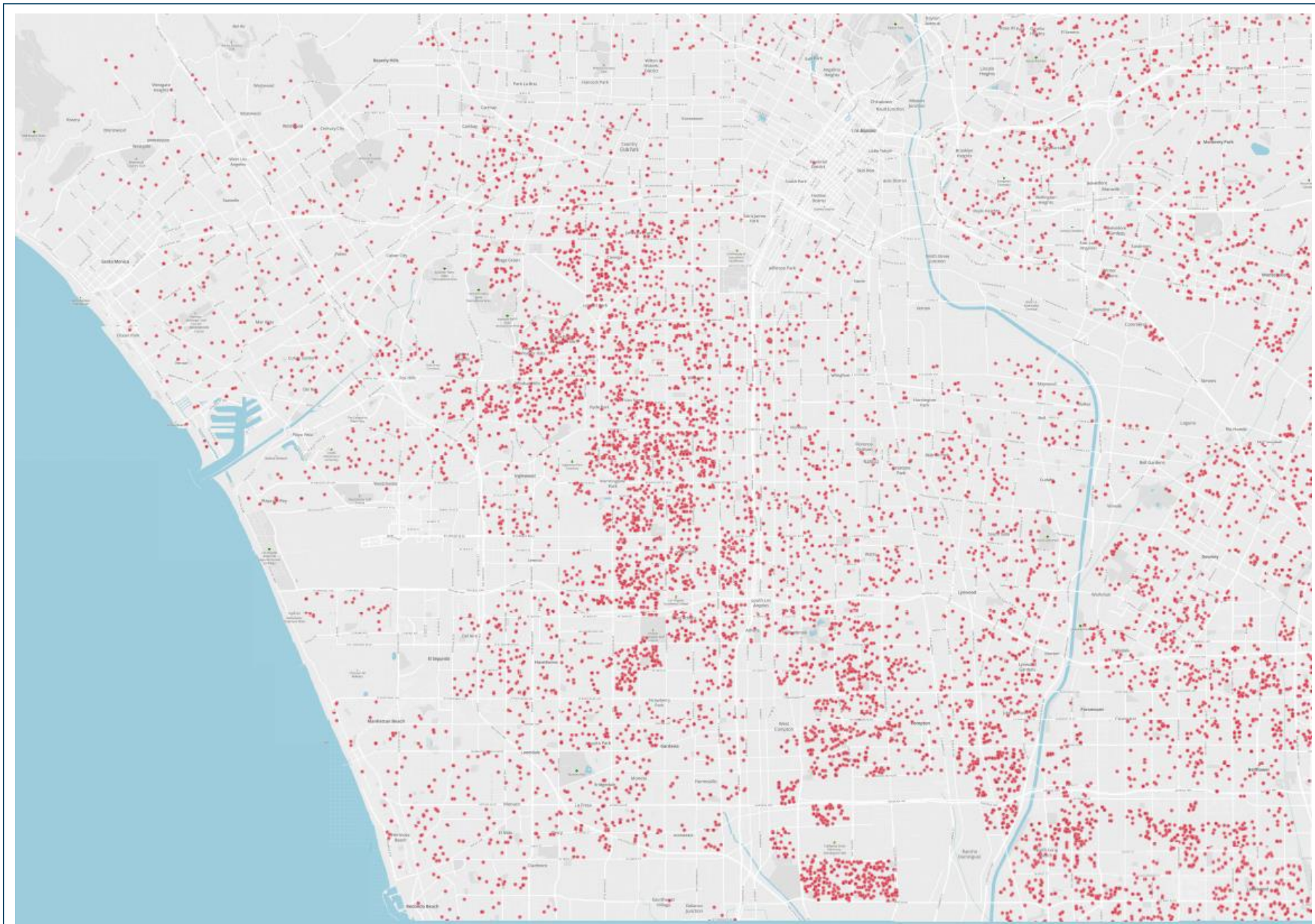
Credit Card: Visa, Master Card, American Express, Discover

- Unsophisticated homeowners are targeted
- Sense of trust because it's a "program"
- They think it's free anyway
- They never see the paperwork

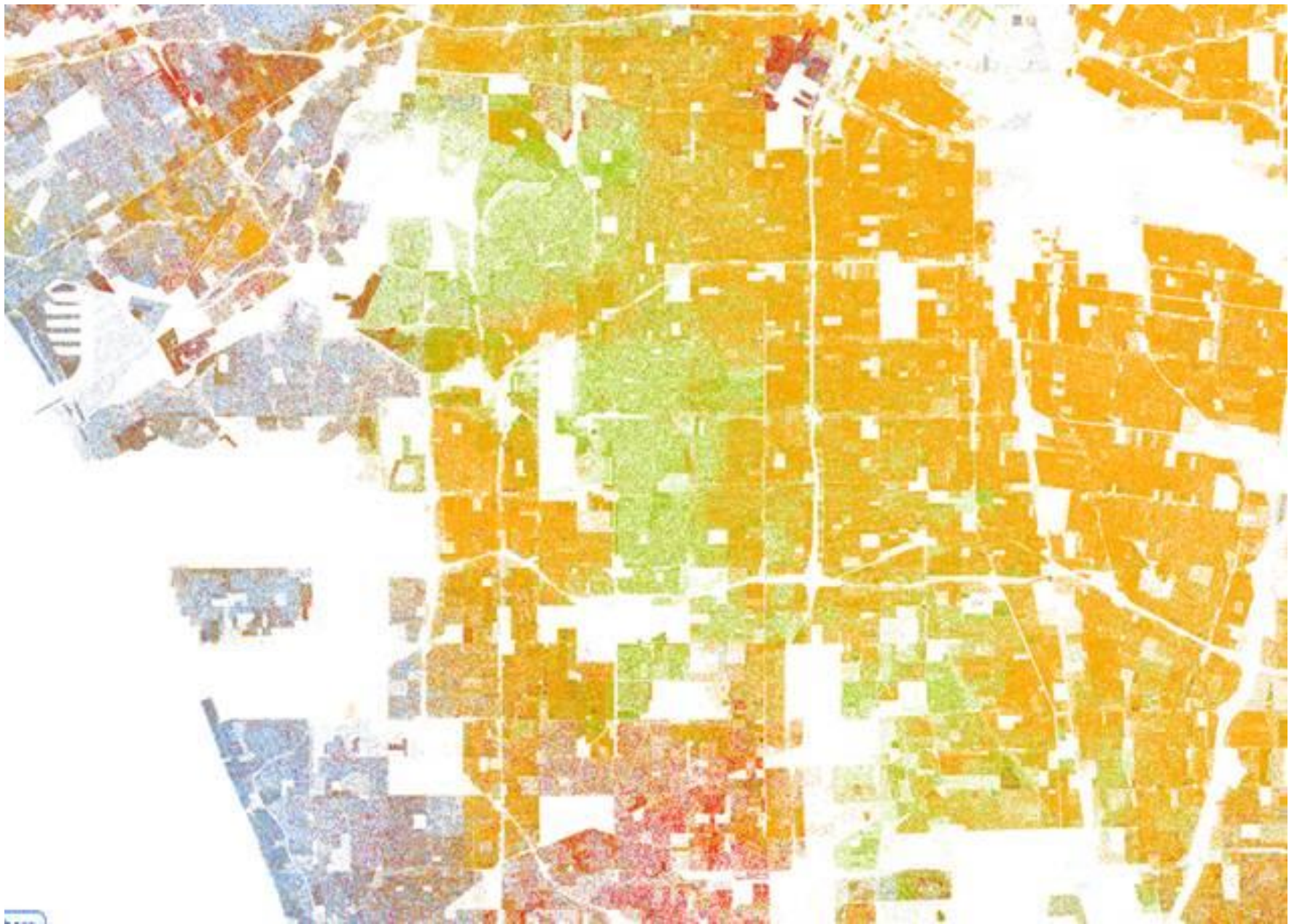
# Language & Race



- Documents are only provided in English
  - E-signing amplifies this problem, with the homeowner fully relying on the representations made by the contractor
- Neighborhoods of color, and particularly African American neighborhoods, seem to be targeted in Los Angeles County.



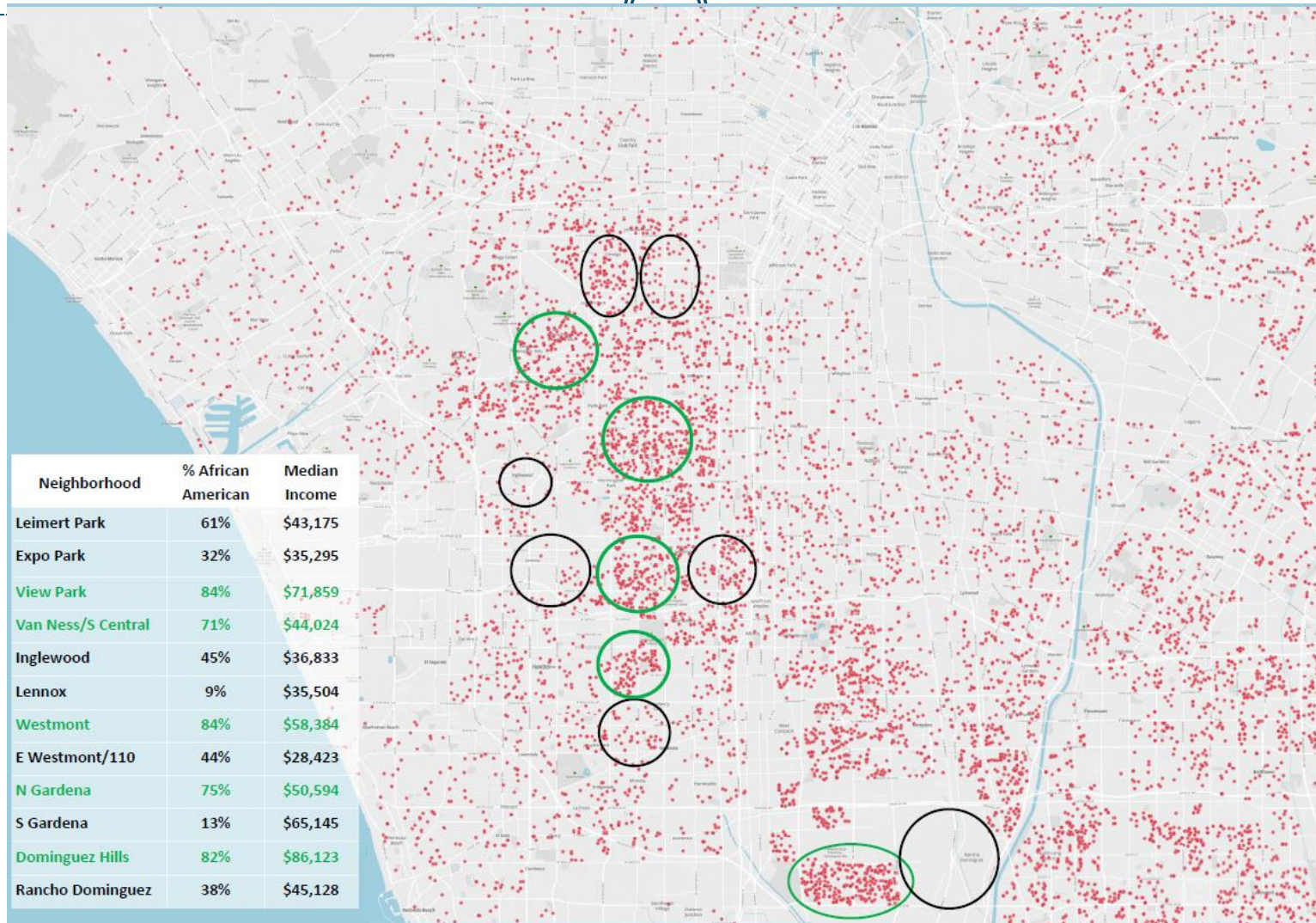




Source <https://demographics.virginia.edu/DotMap/index.html>



(reserved for annotated map, which will look like:)



# Waivers, Arbitration, Lack of Remedies



- By structuring PACE loans as tax assessments, PACE lenders seek to evade consumer protection laws (TILA, RESPA, FTC Holder rule, etc.).
- State enabling statutes lack any remedies.
- Assessment contracts include jury trial waiver, forced arbitration clause, and a class action waiver.
- Contracts also include broad releases of virtually all claims related to the transaction.



# Federal Response



- Congress
  - S.838 - PACE Act of 2017 (Sen. Cotton)
- Department of Energy
  - Best Practice Guidelines for Residential PACE Financing Programs
- Federal Housing Finance Agency (FHFA)
- Consumer Financial Protection Bureau (CFPB)

# California Legislation



## **AUTHORIZING LEGISLATION**

AB 811 (2008): Amends Improvement Act of 1911

SB 555 (2011): Amends Mello-Roos Act

## **ATTEMPTED LEGISLATIVE FIXES**

SB 96 (2013): PACE Loss Reserve Program

AB 2693 (2016): Disclosures and 3-Day Right to Cancel

SB 242 (2017): Limited Consumer Protections

AB 1284 (2017): DBO Regulatory Authority

# Origins



- AB 811 (2008)

- Amendment to the Improvement Act of 1911

- ✦ Improvement Act traditionally authorized the use of assessment powers by local governments to fund projects with a “public purpose”: Streetlights, sewer systems, underground utility lines
- ✦ Expands use of assessment powers for energy efficient improvements to address global climate change = “voluntary contractual assessments”

California Streets and Highways Code § 5898.14

- SB 555 (2011)

- Amendment to the Mello-Roos Community Facilities Act of 1982

- ✦ Provides alternative statutory framework for PACE financing programs
- ✦ Property owners agree to annex properties into a CFD and pay special tax at the time of financing

California Government Code § 53328.1

# PACE Eligibility



- Basic PACE Eligibility Requirements
  - (1) Loan (original SB 77 (2010) language; AB 2597 (2014) changed to financing) recipients are legal owners
  - (2) Recipients are current on mortgage and property tax payments
  - (3) Recipients are not in default or in bankruptcy proceedings
  - (4) Financing for less than 15% of the value of the property up to \$700,000, then 10% of the value above \$700,000
  - (5) The property is within the PACE program area

California Streets and Highways Code § 5898.16(a)(2), referencing California Public Resources Code § 26063(a)

# PACE Eligibility



- Basic PACE Eligibility Requirements (continued)
  - (6) The program finances energy or water efficient improvements
  - (7) Products follow energy efficiency retrofit work standards
  - (8) Total mortgage-related debt and PACE financing do not exceed the value of the property

California Streets and Highways Code § 5898.16(a)(2)

- Annual property taxes and assessments cannot exceed five percent of the property value

California Streets and Highways Code § 5898.16(a)(1)

# CAEATFA



- California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA)
  - SB 77 (2010): Intended to assist local jurisdictions
  - SB 96 (2013) established PACE Loss Reserve Program
    - ✦ Attempt to address FHFA concerns
    - ✦ Mitigate potential risk to mortgage lenders for homes financed with PACE liens by making the first mortgage lender whole for any losses in a foreclosure or forced sale



CALIFORNIA ALTERNATIVE ENERGY AND ADVANCED TRANSPORTATION FINANCING AUTHORITY

# AB 2693 (2016)



- PACE Preservation and Consumer Protections Act

- Provides for three-day right to cancel the assessment contract without penalty or obligation

- ✦ *But* liability may still exist for the underlying home improvement contract = risk of mechanics' lien

California Streets and Highways Code § 5898.16(b)



HERO Financing Program™ Right to Cancel

- Disclosure requirements, including a complete financing estimate

California Streets and Highways Code § 5898.17

NEW

# SB 242 (2017)



- Aligns the home improvement contract and PACE assessment contract right to cancel
  - Home improvement work cannot start until the right to cancel period for the PACE assessment contract has expired; renders contract unenforceable
- “Plain language” oral confirmation of financing terms
  - Preferred language and translated documents requirements
- PACE administrator data reporting requirements
- Prohibits giving contractors information about the amount of PACE financing available for a property
- Prohibits unverified representations about tax deductibility
- Advocates prevented **TERRIBLE** language (e.g. limitation of liability for PACE administrators) from being included in final bill



NEW

# AB 1284 (2017)



- Introduced late in legislative cycle (August 2017)
- Provides for licensing and regulatory oversight of PACE program administrators by the Department of Business Oversight (DBO) under California's Financing Law
- Requires Ability to Repay assessment based on property owner's income, assets, and debt obligations
  - But not before owner commits to financing; only prior to funding and recordation by a public agency of the assessment contract
  - PACE administrators "responsible for the difference"
  - Provides for "emergency" exemptions

# The Future of PACE



- PACE administrators claiming victory – will the legislation allow PACE to expand without critical protections in place?
  - “AB 1284 and SB 242 effectively creates a brand-new PACE product in California – ensuring long-term viability here and serving as a model for PACE to grow responsibly in other states.” *Ari Matusiak, Chief Strategy Officer at Renovate America*
- Significant consumer protection gaps remain, leaving vulnerable homeowners at risk
  - “Concern that PACE may represent the next mortgage crisis-in-waiting has fueled the willingness of this bill’s supporters to overlook its flaws.” *California Senate Committee on Insurance, Banking, and Financial Institutions Analysis of AB 1284*
- PACE is spreading rapidly: MORE WORK TO BE DONE!

# Litigation Strategies



## RECENT DECISIONS IN CLASS CASES

*In re Hero Litigation*  
*Smith v. Ygrene*

## INDIVIDUAL LITIGATION

Elder abuse  
Breach of contract & negligent supervision  
Agency issues  
Defending mechanic's lien cases  
Other claims & considerations

# *In re Hero Loan Litigation*



- Three class actions, in three counties, challenging excessive fees, the calculation of interest and prepayment penalties.
- Claims under TILA, HOEPA and California's UPAP statute.
- “Because California's PACE assessments are tax assessments, because the CFPB has stated that tax assessments are not credit, and because this CFPB opinion as applied to PACE assessments is not demonstrably irrational, PACE assessments are not credit so they are not subject to regulation by TILA or HOEPA.”
  - ✦ *In re Hero Loan Litig.*, 2017 U.S. Dist. LEXIS 111771 (C.D. Cal. July 17, 2017)

# *Smith v. Ygrene*



- California's Consumer Legal Remedies Act does not apply to intangible financial services.
  - Need to show that PACE Administrators have roles beyond that of lenders.
    - Choosing what products qualify for financing
    - Ensuring that only those products are installed
    - Excellent fit with Civ. Code § 1770(a)(5)
- ★ *Smith v. Ygrene Energy Fund, Inc.*, No. 17-CV-01258-LB, 2017 WL 3168519 (N.D. Cal. July 26, 2017)

# These Two Cases



*In re Hero Loan Litigation*

*Smith v. Ygrene*

“It isn’t a loan so TILA and  
HOEPA don’t apply”

“It’s a loan so the  
Consumer Legal  
Remedies Act doesn’t  
apply.”

# Financial Elder Abuse



- Cal. Welf. & Inst. Code § 15600 et seq.
- Taking or assisting in taking the property of an elder
- If you know or should have known the taking was likely to harm the elder.
- “Taking” includes any impairment of a property interest.
  - ✦ See *Bounds v. Superior Court*, 229 Cal. App. 4th 468 (2014).
  - PACE Administrators “take” their own fees,
  - They assist homeowners in “taking” the remainder.
- **Section 15657.5 does not require fraud. Section 15657.6 does not require any wrongful intent.**
- Three potential claims: § 15657.5, § 15657.6, Prob. Code § 859. See also Civ. Code §§ 39, 3345.



# Contracts & Negligence

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(COUNTY)



PACE  
ADMINISTRATOR



CONTRACTORS

- Each of these contracts likely contains consumer protections.
- Third party beneficiary claims under each contract.
- Negligent supervision against (County) for failure to supervise PACE Admins?
  - Check state immunity statute(s)
  - *Doe I v. Wal-Mart Stores, Inc.*, 572 F.3d 677, 682 (9th Cir. 2009)
- Negligent supervision against PACE Admin for failure to supervise contractors.



# Agency Issues



## Find the right contractor, right away.

Finding the right contractor is no small task, so we make the search easy for you. We have a network of experienced local contractors to choose from, all of whom:

- Maintain good standing with HERO
- Adhere to our consumer safeguards
- Are paid only after you sign off on the project



## Verified Contractors

Our network of home improvement contractors are licensed, verified, and are required to adhere to our consumer protection policies.

## 7. How do I explain the HERO Program?

"You are very fortunate because of where you live. Western Riverside County really wants you to be energy efficient, so they've made low cost financing available through their HERO Program."

### ✗ DON'T SAY

HERO will save you money.

HERO provides "free government money" that does not need to be paid back.

HERO payments are transferable to a new owner if you sell.

HERO interest rates are "low" or "affordable."

HERO upgrades will increase your home's property value.

HERO is tax-deductible.

HERO is a government-sponsored, a government-incentive program OR the government can help you pay for the improvement.

HERO is the best borrowing option for homeowners.

You are pre-approved or pre-qualified.

# Beneficial Relationship



- Concentrate on agency as to the loan origination
  - Not the home improvements
- Agency relationship tests will vary state by state
- Tell the story of the practical advantages to the Admins:
  - Introducing the product
  - Putting people on the phone
  - Presenting documents electronically for signature, etc.
  - “Appellant not only relies, but in fact depends on the teachers to act as its conduit to the students ... [and] is thus exploiting or enjoying the benefit of California’s schools and employees to obtain sales.”
    - ✦ *Scholastic Book Clubs, Inc. v. State Bd. Of Equalization*, 207 Cal. App. 3d 734 (1989).

# Defending Mechanic's Lien Cases



- Bring counterclaims
- Name the Admin
- Check the HIC contract
- Get the Admin's copy of the HIC contracts

(Name and Address of Construction Fund Holder)

**DESCRIPTION OF THE PROJECT AND DESCRIPTION OF THE SIGNIFICANT MATERIALS TO BE USED AND EQUIPMENT TO BE INSTALLED:** Direct Contractor will furnish all labor and materials to construct and complete in a good, workmanlike and substantial manner a: \_\_\_\_\_

INSULATED FA HANG ALL TO  
BG ENERGY EFFICIENT - R-38

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INSULATED FA HANG ALL TO  
BG ENERGY EFFICIENT - R-38  
ENERGY EFFICIENT WINDOWS

# Other Theories & Considerations



- UDAP
  - Taxpayer waste
  - Delegation claims
  - Home solicitation statutes
  - Contractor laws
  - Phone banks:
    - TCPA
    - RICO
- Experts
    - Ask your Mortgage Bankers Association
    - Try to find an energy expert
    - Pay for an energy audit?

# PACE Resources



- National Consumer Law Center
  - PACE webpage: [www.nclc.org/issues/pace-loans.html](http://www.nclc.org/issues/pace-loans.html)
  - PACE listserv: <http://lists.nclc.org>
- Energy Programs Consortium
  - R-PACE Primer Report
- PACENation
  - <http://pacenation.us>
- Department of Energy [Best Practice Guidelines](#) for Residential PACE Financing Programs

# Taking Action



- Send NCLC examples of consumer abuses and PACE projects that are not cost-effective
- Ask clients to submit complaints to the CFPB
- Monitor changes to state law and local program requirements