

June 5, 2018

SENT VIA ELECTRONIC MAIL, COURIER

[regulations@dbo.ca.gov; colleen.monahan@dbo.ca.gov]

CALIFORNIA DEPARTMENT OF BUSINESS

OVERSIGHT Legal Division

Attn: Mark Dyer, Regulations Coordinator

1515 K Street, Suite 200

Sacramento, CA 95814-4052

**Re: Request for Comment on Proposed Rulemaking (PRO 02/17) –
Implementation of AB 1284 Licensure of PACE Program
Administrators under the California Financing Law (“Proposed
Rules”)**

Dear Mr. Dyer:

The California MBA¹ appreciates the opportunity to comment on the Department of Business Oversight’s (“Department”) above-referenced proposed rulemaking for implementing of AB 1284 (Chapter 475, Statutes of 2017). In this letter, the California MBA sets forth general recommendations regarding the Department’s approach to proposed rules governing PACE loans and the licensing of Program Administrators, and then gives comment on some specific proposed rules.

I. General Observations Regarding PACE Loan Programs Offered in California

**A. Federal Law Enacted Holding PACE Loans to Truth In Lending Act
“Ability To Repay” Underwriting Requirements for Residential Mortgage Loans.**

¹ 1 The California Mortgage Bankers Association (California MBA) is a non-profit trade association comprised of over three hundred (300) residential and commercial mortgage members, both federally insured depository institutions and California-licensed non-depository lenders, operating in California. California MBA members represent the full spectrum of the California real estate finance industry: loan originators, mortgage bankers, loan servicers, loan investors and securitizers, as well as a broad range of service providers supporting the industry. According to statistics published by the national Mortgage Bankers Association (MBA) for 2017, the estimated dollar volume of residential purchase and refinance loan originations in the United States during 2017 was approximately \$1.710 trillion dollars. Based on historical data, approximately fourteen percent (14%) of those loans (over \$239 billion), were originated in California. Of these, a substantial percentage---if not the majority---were originated and serviced by California MBA members.

Since the Department published the Proposed Rules for comment, Congress enacted and President Trump signed into law the *Economic Growth, Regulatory Relief, and Consumer Protection Act* (S. 2155). Among its provisions, S. 2155 designates Property Assessed Clean Energy (PACE) financing programs as a type of residential mortgage loan product subject to the federal Truth In Lending Act's (TILA) Section 129C(b)(3) "Minimum Standards for Residential Mortgage Loans - Ability To Repay" underwriting requirements. In so doing, S. 2155 directs the Consumer Financial Protection Bureau to draft federal rules in Regulation Z (TILA) for the underwriting of PACE loans subject to ability to repay requirements for residential mortgage loans. Further, S. 2155 holds PACE program administrators subject to the enforcement provisions of TILA Section 130 (15 USC 1640) when committing one or more violations of TILA's Ability To Repay underwriting requirements in a PACE loan transaction.

With the passage of S. 2155 and the Bureau's impending Ability To Repay rulemaking for PACE loans nationwide, the Proposed Rules need to be modified in two material ways, while remaining consistent with AB 1284's addition of "ability to repay" underwriting requirements for PACE loans found in California Financial Code ("FC") Sections 22686 and 22687, as well as the enforcement provisions found in FC Sections 22714(a)(4) and (a)(5).

(1) Express recognition that PACE financing programs are to be treated under state law as consumer purpose, residential mortgage loan products. **The Proposed Rules lack a definition for what constitutes a "PACE Loan program;"** and

(2) Express requirement that PACE loans are to be underwritten in conformity with federal ability to repay rules for residential mortgage loan transactions under Truth In Lending Act Section 129C (15 USC 1639c) and its implementing Regulation X (12 CFR §1026.43). This requirement can be covered through **Proposed Rules Section 1620.21 Property Owner Protections, Section 1620.22 Property Owner Income, Section 1620.23 Other Assets, Section 1620.24 Basic Household Living Expenses, and Section 1620.30(b) Application for a Program Administrator License.**

B. California's 2018 Legislature Is Considering Further Reform Enhancements for PACE Loan Programs under SB 1087 (Roth) and AB 2063 (Aguiar-Curry).

The California MBA further wishes to acknowledge that the California Legislature is considering two bills this session that would go further than AB 1284 in the areas of consumer protection for California homeowners shopping for and securing PACE loan financing for their homes. **The California MBA supports both bills and requests the**

Department to begin the drafting of enhanced PACE regulations adding even greater consumer protections, disclosures and publicly available data on PACE loan programs offered and secured by California homeowners.

SB 1087 (Roth) would add more rigorous requirements for PACE Administrators when originating PACE financing, such as additional consumer protections and/or tighter underwriting requirements. As of May 25, 2018, SB 1087 moved out of the Appropriations Committee to the Senate floor for a full vote.

AB 2063 (Aguiar-Curry) would also create several new requirements for PACE solicitors and PACE Administrators that would provide additional protections for California borrowers. California MBA views these proposed changes positively. AB 2063 changes would include:

- Prohibiting a person from engaging in the business of a PACE solicitor unless that person is enrolled with a program administrator in a manner that is acceptable to the Dept of Business Oversight commissioner.
- Prohibiting a program administrator or California homeowner from executing an assessment contract, and would prohibit any work from commencing under a home improvement contract that is financed by that assessment contract, unless the program administrator ensures that specified criteria related to that assessment contract are satisfied including a reasonable and good faith determination made by the program administrator that the property owner has a reasonable ability to pay the PACE loan assessment.

As of May 25, 2018, AB 2063 passed the State Assembly and is pending with the Senate.

C. The Proposed Rules Do Not Establish A Public Registry for Tracking PACE Assessments As Required by AB 1284.

Of great concern to California MBA and its members is the current lack of public notice when a PACE assessment is placed on a California home. The existence of a PACE assessment and its disclosure on a property tax assessment and title policy in a clear, uniform and readily identifiable manner are material to our membership for underwriting mortgage loan applications in compliance with TILA and Regulation Z “ability to repay” requirements, property lien and title policy reviews, as well as for federal and state mortgage servicing and escrow accounting laws and rules covering collection of consumer debts and payment of property taxes through escrow accounts.

Title and escrow companies have expressed similar concerns to our membership. They indicate that PACE assessments are not consistently and expressly being reported on property tax rolls, and sometimes are mischaracterized as being another type of assessment such as Mello-Roos.

A public database administered by the Commissioner is necessary for all interested parties to a PACE loan program, to California homeowners, and to the mortgage industry. The 2017 California Legislature recognized this as an urgent issue in AB 1284 and added Financial Code Section 22693 accordingly:

(a) The [C]ommissioner may, by rule, require a program administrator to use a real-time registry or database system for tracking PACE assessments in order to carry out his or her regulatory duties and to support enforcement. That registry or database system shall enable the program administrator to trace PACE assessments and shall include, but not be limited to, features for providing or obtaining information about a property's status with regard to PACE assessments placed on the property, whether recorded or not. ... The [C]ommissioner may contract with an independent third party for the development and ongoing maintenance and support of the real-time registry or database system, and may require the program administrators to pay the cost of development and ongoing maintenance and support directly to the independent third party.

California MBA respectfully requests the Department to take up this vital project, to activate a public database or registry reporting on PACE assessments placed on California homes that is financially supported by PACE licensees and accessible to mortgage lenders, mortgage servicers, title insurers and agents, independent escrow agents, PACE program administrators and by California homeowners themselves.

D. California MBA Suggests Addition of a Rule Establishing Qualifiers for PACE Loan Eligibility

California MBA and its members believe the Department rules need to set forth a list of qualifiers for borrower and subject property eligibility for PACE Loan financing in order to provide California homeowners adequate protection from untoward sales practices and unaffordable loans. We have already recommended the Department rules expressly require adherence with TILA “Ability To Repay” underwriting requirements. The following are additional qualifiers we feel are necessary for inclusion in Department rules including the proposed **Section 1620.03 Obligations of Program Administrator, Section 1620.06 Mandatory Brochure.**

(1) **Prior Notice of proposed PACE Loan financing to Mortgage Holders and their Servicers according to preliminary title report.** PACE Loan financing is a disqualifier for FHA insured mortgage loans, as well as Fannie Mae and Freddie Mac mortgage loans, and can be a disqualifier for additional government guaranteed and portfolio mortgage loans depending on terms and conditions. In addition, if a subject property carrying PACE financing is sold in the future or if the homeowner wishes to secure cash-out refinancing of their primary mortgage loan, the PACE Loan must be paid off in full before a buyer can purchase the property using FHA, Fannie Mae or Freddie Mac loans as their purchase money financing. As a result, placing a PACE Loan assessment on a subject property without prior consult and approval with the mortgage holder and their servicer may place the homeowner at risk of a loan default event and foreclosure. The Regulations must include a requirement that the homeowner first give advance notice of a planned PACE Loan assessment on a subject property to the mortgage holder and its servicer and receive, in return, written terms of approval to proceed.

California MBA requests the Department to adopt additional rules holding PACE program administrators accountable for early notification and requested approvals from the mortgage lienholder of record and their servicing agent. A homeowner should not be made contractually liable for a PACE Loan without securing the approval and the PACE Loan itself should be rendered void if originated outside the terms of a mortgage lienholder and their servicing agent's consent or lack thereof.

(2) **Disqualification of Certain Subject Properties from PACE Loan financing.** Residential properties that have been constructed by non-profit entities, such as Habitat For Humanity homes, come with homeowner limitations such as debt load. Other residential home purchases are subsidized by federal, state and local assistance programs that come with homeowner limitations. In this regard, the California MBA suggests that PACE Loan financing not be eligible on non-profit and government-subsidized housing without a release of conditions, executed by an authorized representative of the non-profit or government entity, and recorded in the applicable county recorder.

(3) **Equity Preservation.** The combined loan-to-value (CLTV) ratio for outstanding mortgage debt coupled with proposed PACE Loan financing should not exceed 97%, consistent with Cal. Financial Code Section 22683(i). This qualifier gives justification for the valuation requirements and should be incorporated into **Proposed Rulemaking Section 1620.21 Property Owner Protections.**

(4) **Make PACE Loans subject to California "Covered Loan" Limits.** For reasons set forth above, PACE Loans are acknowledged by federal law now to be a type of residential mortgage loan program. California, in an effort to restrict predatory lending practices against California homeowners, places restrictions on certain residential mortgage

loans defined as “Covered” under Cal. Financial Code Sections 4970, *et seq.* That Chapter restricts the amount of interest, annual percentage rate, and costs that can be charged to California homeowners, and it restricts certain terms of a mortgage loan such as prepayment penalty. The Proposed Rules currently place no restrictions on PACE Loan terms such as these. California MBA recommends that PACE Loans and Program Administrators be expressly required to comply with California “Covered Loan” Law provisions through **Section 1620.03 Obligations of Program Administrator, Section 1620.06 Mandatory Brochure and, for non-compliance events, Section 1620.10 Unfair Business Practices.**

(5) **Express Adherence to Cal. Civil Code Section 1632(b)(4).** While Department rules make reference to negotiating PACE Loans in a language other than English (*see, Sections 1620.03(c), 1620.20*) there is no express requirement for compliance with Cal. Civil Code Section 1632 when negotiating PACE Loan programs in the protected languages of Spanish, Chinese, Tagalog, Vietnamese, or Korean. California MBA recommends that PACE Loans and Program Administrators be expressly required to comply with California Civil Code Section 1632(b)(4) in these Sections.

(6) **Mandatory Homeownership Counseling Prior to PACE Loan Origination.** In AB 1284’s framework, PACE Loans are to be solicited to California homeowners by sponsored sales agents who are licensed contractors seeking to be hired to perform the desired home improvement. That is a fundamental conflict of interest - having a financial interest in the origination of a PACE Loan transaction. For this reason, the California MBA recommends that California homeowners complete homeownership counseling by an independent, certified counselor who can present the homeowner with three or more financing options (such as unsecured loans, home equity lines of credit and cash-out mortgage refinancing offering better rates and terms than PACE Loan programs), before the homeowner can become contractually obligated on a PACE Loan.

II. Comments Specific To Proposed Rules

A. Section 1620.02 Definitions.

- (a) “Ability To Repay” definition should be revised to incorporate the components of a TILA Regulation Z “ability to repay” underwriting reviews set for the in 12 CFR 1026.43(c), namely: income, assets other than subject property value and available equity, debts including all mortgage obligations including PACE Loans, debt-to-income ratio and credit history.
- (c) This subsection is not a definition but rather, a continuation of subsection (b) definition, “Authorized by a program administrator.”
- (d) “To solicit a property owner” definition. Due to the inherent conflict of

interest concerns California MBA has with licensed contractors acting as PACE Loan sales with a requirement that the homeowner complete homeownership counseling with an independent and certified third party counselor who can present the homeowner with alternative financing options. Homeownership counseling must be completed before a homeowner can become contractually obligated on a PACE Loan.

B. Section 1620.03 Obligations of Program Administrator.

(c) As explained above, California MBA requests the Department add an express requirement of adherence to Cal. Civil Code Section 1632(b)(4).

C. Section 1620.04 PACE Pricing.

We request removal of “common” in the second line.

D. Section 1620.05 Advertising Standards, 1620.06 Mandatory Brochure

California MBA has identified additional advertising disclosure items to be added to this proposed Section 1620.05 as well as Section 1620.06 Mandatory Brochure. They are:

(1) **Advertising, Consumer Complaint Disclosure.** California MBA recommends that the Department include in its PACE rules a requirement that any PACE Loan program literature, whether written, electronic or audio, include the Department’s standard licensing disclosure language for program administrators and instruction to consumers on how to contact the Department for complaints, questions and concerns.

(2) **Explain the Nature of PACE Loans.** California MBA recommends all advertising including a disclosure that PACE Loans are a residential mortgage loan with superlien priority via property tax assessments. Interest accrues on a PACE Loan for the life of the loan. PACE Loans are not government loans. Rather, they are sponsored by local governments and originated by for-profit program administrators licensed by the California Department of Business Oversight under the California Finance Lenders Law. Failure to timely repay PACE Loans through property tax assessments can result in late penalties, an event of default on the primary residential mortgage loan and, if not corrected, possible foreclosure of the home.

(3) **Caution for Mortgage Loans With Impounding For Taxes.** If impounding for property taxes through the primary mortgage loan, the homeowner should be aware that their monthly mortgage payment will increase commensurate with the increase in property tax assessment.

(4) **Caution for FHA Loans.** As described above, California MBA recommends advertising disclosure caution homeowners that PACE Loans are not eligible on homes with FHA mortgages and may be ineligible for other primary mortgage loan programs.

The homeowner must first receive confirmation from their mortgage holder and servicer that PACE Loans can be placed on the home before they can become contractually obligated for repayment on a PACE Loan.

E. Further Comments re Section 1620.06 Mandatory Brochure

(a)(2) California MBA suggests the requirement that California DBO give prior approval to each brochure created by a program administrator is unnecessary so long as the regulations add specificity to what information and disclosures must be included in the brochure, and the Department has internal mechanism for receiving consumer complaints regarding perceived unfair business practices including advertising

(c)(7) As explained above, while suggesting to consumers that they consult their tax advisor before entering into a PACE Loan transaction, the California MBA recommends that California homeowners be required to complete homeownership counseling with a certified counselor as a precondition to becoming contractually obligated for a PACE Loan.

F. Section 1620.07 Books and Records.

California MBA requests the Department to add to the list “Evidence of written notification to mortgage lienholders of records and their servicing agent of a proposed PACE Loan financing; written notice of consent to proceed from the mortgage lienholder and/or their servicing agent.”

G. Section 1620.10 Unfair Business Practices.

Consistent with our previous comments, the California MBA recommends that an event of non-compliance with each of the qualifiers proffered be included as additional UBP events in Department rules.

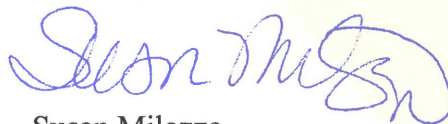
H. Section 1620.11 Solicitor Enrollment Standards or Processes

(a)(3)(G) Regarding solicitor agent training being conducted in compliance with FC 22681, the California MBA suggests that this rule add a continuing education requirement in addition to the initial six-hour training prescribed by statute. PACE solicitor

agents will need to stay up to date on changes to laws, rules and prescribed “best practices” for safe and ethical PACE lending going forward. We suggest the continuing education be a minimum four (4) years every year to two years.

We thank you for your consideration of these views. Please reach out to me if you have any questions concerning our comments or need further information.

Sincerely,



Susan Milazzo
Chief Executive Officer
susan@cmba.com
(916) 446-7100