BET TZEDEK
JUSTICE FOR ALL

January 5, 2018

VIA EMAIL AND U.S. MAIL
California Department of Business Oversight
Attn: Mark Dyer, Regulations Coordinator
1515 K Street, Suite 200
Sacramento, CA 94105
Regulations@dbo.ca.gov

Re: Comments on Proposed PACE-Related Rulemaking for Implementation of AB 1284; File No: PRO 02/17

Dear Commissioner et al:

Thank you for the opportunity to comment on the Department of Business Oversight's Rulemaking for implementation of AB 1284 (Chapter 475, 2017). We do so in our capacity as one of California's leading public interest law firms, with 40 years of experience providing comprehensive legal services for low-income individuals and families in Los Angeles County and City.

In the past year, Bet Tzedek has experienced a dramatic spike in elderly and disabled clients whose homes are threatened by overwhelming PACE loans that they are unable to pay. We, as well as the additional undersigned organizations, have become very familiar with the PACE program. Although the PACE program is a potentially beneficial financial tool, because of lack of regulation and oversight, we have unfortunately seen the misuse of this program by both PACE administrators (used interchangeably with "program administrators" herein), PACE solicitors, and home improvement contractors (who often act as PACE solicitors or solicitor agents).

With the passage of AB 1284 and SB 242 (Chapter 484, 2017), the California legislature took an important step toward ensuring that consumers of PACE financing are being protected from unscrupulous and unfair business practices. However, the signatories to this letter take the position that these regulations do not go far enough to protect consumers in an industry where the stakes for loan default are so high. The patterns we have seen in our clients' experiences put us in a unique position to comment on AB 1284, SB 242, and the rulemaking needed to make the DBO an effective regulator for this industry. We hope that the DBO will find our experiences helpful in illustrating where rulemaking is needed to protect consumers from financial fraud and make PACE financing a tool worthy of the municipal resources that fund it.

In addition to concurring with the recommendations in the joint Comments on Proposed PACE-related Rulemaking from the California Low Income Consumer Coalition (of which Bet Tzedek is a member), the lending community, the real estate community, and others (the "Coalition Letter"), we the undersigned wish to further highlight and illustrate a few key areas ripe for rulemaking.

Definitions - § 22017

In section 22017, "PACE solicitor" is defined as a person authorized by a program administrator to solicit a property owner to enter into an assessment contract. This is a circular definition that needs clarification. What does it mean to solicit?

In our experience with clients, consumers first interface with a home improvement contractor who solicits home improvements. The first contract they sign is a home improvement contract, which may or may not reference PACE or assessment contracts. The assessment contract itself is typically signed separately, at a later date, and may be received by the consumer via mail or email, or be presented to the consumer on a tablet or smart phone by the same or a different person than the initial home improvement contractor.

To "solicit" under § 22017 should be defined broadly, to include anyone who offers home improvements that are financed by PACE and/or discusses PACE financing with consumers as a financing option for their home improvements. If a home improvement contractor receives a payment directly from a program administrator, that should create a presumption that they are a PACE solicitor within the meaning of § 22017.

Annual Report Data - § 22159

PACE loans are creatures of statute. PACE administrators are government contractors and rely on government entities to enable PACE lending and collect and remit PACE loan proceeds. Because of the government's role in PACE, it is especially important that detailed data about the PACE program and PACE administrators be available to the public. In investigating our own clients' claims, we have been stymied in trying to discover information relevant to the integrity of the PACE transactions at issue, including data related to where and when electronic signatures were made, or whether any other complaints have been made against a particular contractor. We believe that PACE consumers should have a right to all the supporting documents and correspondence related to their individual PACE transaction, including correspondence between the PACE administrator and PACE solicitors or solicitor agents.

On an aggregate level, the reporting data required by § 22159(a) should include the data needed to determine if AB 1284 and SB 242 are working to protect consumers. Comprehensively tracking foreclosure, delinquency and default data is one metric that can be used as a proxy for determining whether AB 1284's ability to pay formula is robust enough, and being followed.

In many cases, foreclosure, delinquency and default can be masked by the involvement of a third-party lender. In the case of consumers with reverse mortgages, for example, the lender is required to pay delinquent property taxes before default, to protect the lender's lien priority. For those with conventional mortgages with an impound account, the lender always pays the annual tax bill in full, and passes that debt on to the homeowner after an escrow analysis.

These interventions by third-party lenders following the imposition of a PACE assessment should be tracked. At the time of application, PACE administrators, their solicitors or solicitor agents should be required to ask potential customers if they have a reverse mortgage or a conventional mortgage, and who the lender is. PACE administrators should also be required to report any property that has had a title change since the PACE lien was impressed (as a way to track bank foreclosures vs. tax defaults).

Tracking price data for PACE-eligible products and services is also critical to consumer protection. Currently, there appear to be no cap on what a contractor can charge a customer for any PACE-eligible product. Bet Tzedek has experienced sticker shock in its review of many of these transactions, with prices that appear to have been approved without question by the PACE administrators. In one case, for example, a consumer was charged over $40,000 for an HVAC system for an 1800 square foot house. On further inspection, the system installed was of commercial grade, was installed on the roof, and became a fire hazard. Windows and insulation are another area where unconscionable overpricing seems to go unchecked. One client was charged $8,000 for 4 windows. Another was charged over $30,000 for foam insulation of a 2700 square foot house. We were unable to find any data to justify $30,000 as a competitive market rate cost of insulation for a home of this size.

We hope that this will change with implementation of Section 5926 of the Streets and Highways Code (SB 254), which prohibits contractors from providing a different price for a project financed by a PACE assessment than the contractor would provide if paid in cash by the property owner.

To ensure that § 5926 accomplishes its purpose, PACE solicitors should have to provide program administrators with their cash pricing, and PACE administrators should have to report what they pay contractors for similar products across different projects, including quantity, mean, median, average cost per square foot, and standard deviation of distribution. If they utilize internal pricing guidelines, these should be reported publicly as well. This data will not only deter unfair overpricing, but it will give consumers a public resource to compare their project pricing against, and give lawmakers the tools they need to assess the value of the home improvements being offered through the PACE program.

<u>Complaint Processes and Procedures - § 22683</u>

Section 22683 is a critical regulation, but it is vague. When it states that the program administrator shall develop and implement policies for responding to complaints "as soon as

possible," does that mean the policies themselves should be developed ASAP or that the policies should provide that complaints be responded to ASAP? What does "reasonably practicable" mean, and who determines that? We suggest that complaints be responded to within 60 days or within 30 days of the date the next PACE installment payment is due, whichever is sooner. If a consumer is facing irreparable harm, like foreclosure, there should be a mechanism for expediting complaints.

A consumer complaint of fraud, forgery, or problems with workmanship should automatically trigger an investigation.

DBO should mandate that PACE consumers have a right to access to their entire client file, including any and all communications (including electronic) between themselves and the program administrator, and between the program administrator and the PACE solicitor or solicitor agent. This policy will help uncover preventable fraud, like a PACE solicitor having provided one contract to the property owner and a different contract to the program administrator, for example.

Complaints should be documented, including identifying the nature of the complaint. In addition, all of the complaint information, including the number of complaints, the PACE solicitor or solicitor agent involved in each complaint, and how the complaint was resolved, should be part of the annual data that program administrators are required to report under § 22159(a).

DBO should also implement an appeals process for complaints that are not resolved timely, or not resolved to the consumer's satisfaction. We support the suggestions provided in the Coalition Letter on this issue.

Periodic Review Standards - § 22680(e)(3)

When a PACE administrator conducts a periodic review of its PACE solicitors every two years as required by § 22680(e)(3), it should confirm that the solicitor continues to meet the requirements of § 22680(c). The program administrator should also review its complaint log to see if the solicitor was the subject of any complaints in the past two years. If a solicitor was the subject of two or more complaints involving misrepresentations, overcharging, fraud or poor workmanship, they should be de-enrolled. Program administrators should also examine a random selection of 2-4 transactions from each PACE solicitor to assess whether the solicitor demonstrates competency with the training materials required by § 22681, are pricing their projects in accordance with Streets and Highways Code § 5962, and remain in compliance with § 22680(d).

Ability to Pay - § 22687(a)

Section 22687(a) states that prior to funding and recordation of a PACE assessment, a program administrator must determine whether the property owner has a reasonable ability to meet the annual payment obligations for the assessment. This ability to repay determination should be responsive to the unique way in which payment obligations for PACE loans are structured. For those consumers who own their homes outright, have a conventional mortgage but do not impound their taxes, or have reverse mortgages, they will be required to pay their PACE loan in two lump sum payments, at most four months apart, in December and April.

Different property owners are in different situations. For example, consumers who own their homes outright, have a conventional mortgage but do not impound their taxes, or have reverse mortgages, will be required to pay their PACE loan in two lump sum payments, at most four months apart, in December and April.

In addition, depending on when in the calendar year the PACE loan is funded, a homeowner may be required to make their first payment immediately, or may not have to make a payment for another calendar year. For example, a person whose PACE assessment is funded in June will likely have to make her first payment by December 10th of that same year, whereas a person who contracts in December won't have to make any payments until the following November, because the tax year runs from July to July. Thus, the timing of the assessment contract can greatly impact whether a consumer has the "ability to pay" the annual assessment (at least in the first year). Rulemaking should reflect the reality that consumers need to have access to a lump sum payment of thousands of dollars (our clients' average annual assessment is $6,300) within weeks or months of signing the assessment contract.

For those consumers who have a conventional mortgage with a tax impound account, their taxes will be paid directly by the services and then paid monthly by the consumer through an increased escrow payment. The increased escrow payment will in most cases significantly exceed 1/12 of the annual PACE assessment since increases in a property tax bill generally generate a new escrow shortage and/or deficit, and increase the permitted two-month escrow account cushion servicers are permitted to collect. Section 22687(d)(2) includes mortgage payments in the ability to repay analysis, but it should be clear that to meet the "annual payment obligation," the ability to pay analysis for a person with a conventional mortgage must consider the escrow shortage that the PACE loan will create.

Any forms to be completed by the property owner in making the ability to repay determination should be in simple, easily-understandable language with a large, readable typeface to minimize the likelihood that an unsophisticated or less educated homeowner will make an error that might later be characterized as an intentional misrepresentation under § 22687(g). Forms should be available in the same language in which the PACE transaction was negotiated.

Housing Expenses - § 22687

Section 22687(b)(2)(c) defines monthly debt obligations to include all secured and unsecured debt, alimony, child support and monthly housing expenses. Section 22687(d)(4) states that a homeowner shall have sufficient residual income to meet "basic household living expenses" which the PACE administrator may make a "reasonable estimation" of, based on the number of people in the household. Rulemaking should clarify that if a consumer can document their monthly expenses, the PACE administrator should rely on that rather than its own "reasonable estimation." If a PACE administrator does employ a "reasonable estimation" model, it should have to document what inquiries it made to the consumer, and what costs it considered for the expenses and residual income analysis. PACE administrators should also have to make this documentation available to the consumer, and DBO.

In addition, rulemaking should require that PACE administrators inquire as to caregiving, caretaking, and medical expenses and debt. For many of our clients, medical expenses and the costs of caring for others or being cared for themselves, are a major financial burden. For an elderly person who requires at home caregiving, that expense is a housing expense in the sense that without such assistance, the individual would not be able to remain safely in their home. In addition, many of our elderly and disabled clients have incidental and ongoing expenses that may not be captured by a generalized estimation of living expenses.

Repayment for Misapplication of Ability to Pay Standard - § 22687(g)

An ability to pay analysis should be performed before any extension of credit is made. The "finance first, evaluate later" model that is implied in AB 1284 is unlikely to prevent the extension of credit to homeowners with inadequate ability to pay. Section 22687(g) provides a potentially powerful remedy for low-income homeowners. As currently written, however, the provision lacks the necessary teeth. Rulemaking should require that program administrators refund any difference between what the property owner can pay and the actual amount financed, within five business days. Given that this determination is required to be made before recordation, pursuant to § 22687(a), the refund may be in the form of a reduction in the total assessment amount that is ultimately recorded.

The language about a homeowner's intentional misrepresentation should be clarified to make clear that what is meant is an intentional misrepresentation about income or expenses, the data forming the basis of the ability to pay analysis. Misrepresentations made to the consumer by the PACE administrator or PACE solicitor in the process of obtaining ability to pay analysis data should be a defense. Rulemaking should also provide for an appeals process for this determination. Recordation of the PACE assessment should be held in abeyance pending resolution of the appeal.

Emergency Exception - § 22687(e)(4)

We believe that § 22687(e)(4) requires rulemaking to avoid abuse. First, we urge DBO to clarify the definition of "emergency or immediate necessity" to make clear that this is a narrow exception, applicable in limited circumstances of true urgency, and cannot be used to circumvent the protections of AB 1284 generally. For example, while an HVAC system may qualify as an emergency in some parts of California in July, it is hard to see when air conditioning would ever be necessary on an expedited basis in December. We also suggest that the phrase "system whose primary function is temperature regulation" be further defined to exclude non-emergency improvements that may (at least arguably) regulate temperature, like light-reflective paint.

The waiver of the right to cancel in § 22687(e)(5) should be required to be in the homeowner's primary language, and wet signed only (no DocuSign or e-sign), to prevent against a common scenario we've seen where consumers are asked to e-sign PACE-related documents on solicitor's own tablet computers or other electronic devices, and are not required (or in some cases allowed) to read the document, and are never given a hard copy for review.

It should also be made clear that the laws against price gouging apply to this emergency exception.

Assessment Database - § 22693(a)

Section 22693(a) allows the commissioner to require a program administrator to use a real-time registry for tracking PACE assessments, whether recorded or not. We believe that a registry of this kind would be a valuable tool to support enforcement of AB 1284. About one in three clients come to us with multiple assessments on their property, sometimes multiple assessments from the same administrator and in other cases competing administrators. In one case, the client ended up with a PACE lien from every administrator licensed to operate in their zip code. However, the PACE solicitor had led the client to believe that each of the home improvement contractors the client worked with were all part of the same "government program for seniors" that they thought they were being enrolled in – they had no idea how they ended up with multiple assessment contracts and tax liens. The multiple assessments together totaled $118,000 for a home valued at $500,000 – over 20% of the home's value – and included overpriced and overlapping work (every contract included "insulation" of some kind). This client's mortgage increased by over $2,000 per month – more than their monthly income - and they are now facing foreclosure. A real-time registry could have limited this client's exposure, and could have led to discovery of the misrepresentations made to the client by the PACE solicitor and solicitor agent's much sooner.

Early documentation of a new PACE loan is critical to an effective assessment database. We suggest that PACE administrators enter a customer into the database as soon as they make an application for PACE financing (or re-financing). At a minimum, the PACE assessment should

be entered into the database as of the date of funding (i.e., when the Completion Certificate is signed and funds remitted to the contractor).

PACE administrators should be required to check the database before extending funding to a new customer. If a PACE administrator discovers that a potential customer already has a PACE lien reported from another administrator, the administrator should have to perform a due diligence review of the assessment, determine if the second assessment is for unique work, and incorporate the pre-existing (or pending) PACE loan debt into the ability to pay and residual income analysis.

Term of Repayment - § 22684(g)

Section 22684(g) currently requires that a program administrator not submit an assessment contract unless the measures to be installed pursuant to the assessment contract are eligible for PACE financing. In our experience, it is rarely the case that the assessment contract lists an item that is not eligible for PACE funding. However, we see ineligible work performed in nearly all of our cases. What is missing is a system of accountability where the PACE administrator confirms that the work that was actually performed was PACE eligible (whether it is reflected on the assessment contract or not). We have many cases where consumers were misinformed by PACE solicitors that the PACE program could be used for kitchen remodels, for example - an outcome that may increase consumer interest in PACE financing, but makes a mockery of the program's environmental mission.

Program administrators should also have to confirm that the items to be installed pursuant to the assessment contract were in fact installed. We have several clients whose assessment contracts purport to involve extensive replacement of windows and insulation of attics, floors and walls, which were never completed or completed with fewer resources than reported in the assessment contract. Square footage should also be confirmed. We have reviewed assessment contracts for installation of roofs and drought-tolerant landscaping, for example, for areas far exceeding the square footage of the home - information that is publicly available through a simple web search.

Discovery of a discrepancy should automatically trigger the consumer complaint process, and assessment contracts should be revised so that PACE financing is only applied toward eligible products and/or products that were actually installed. As a deterrent and incentive to properly train its PACE solicitors, the program administrator should also be required to indemnify the homeowner against any mechanic's liens imposed for ineligible work that was induced by fraud, forgery, or misrepresentation.

In general, DBO should ensure that consumers and local governments have recourse if program administrators are submitting assessment contracts for recordation that do not meet the appropriately stringent requirements of § 22684.

Thank you for your attention to these comments. We look forward to continuing to work with DBO to ensure a sound model of regulation for PACE financing.

Sincerely,

/s/ Jennifer H. Sperling, Esq.
Bet Tzedek Legal Services

Concurrence by:
Central California Legal Services, Inc.
East Bay Community Law Center
Elder Law & Advocacy
Law Foundation of Silicon Valley
Legal Aid Society of San Diego
Public Counsel
Public Law Center
Riverside Legal Aid