AMERICANS for TAX REFORM

722 12th Street N.W.

Fourth Floor

Washington, D.C.

20005

T: (202)785-0266

F:(202)785-0261

www.atr.org

An Issue Brief on PACE Financing in the States

Property Assessed Clean Energy (PACE) is a government-backed and managed loan program used by private property owners to finance energy efficiency or renewable energy upgrades. This complicated financing scheme involves municipalities creating energy assessment districts and local governments issuing bonds to loan providers. The loans can be issued by third parties, but are secured by a property tax lien and collected through municipal tax bills, attaching the loans to the property and not the person.

The first PACE program was implemented in Berkeley, California *in an effort to address climate change* by providing a no-cost up-front option for homeowners to make alternative energy upgrades to their property.

Five Things You Need to Know About PACE Financing

1. **There are Significant Consumer Protection Questions.**
Since PACE financing is not structured as a loan, but as a tax assessment, the programs are not currently required to disclose financing costs like traditional lenders, and loan providers are not subjected to Truth in Lending requirements. Sens. Tom Cotton (R-Ark.), Marco Rubio (R-Fla.) and John Boozman (R-Ark.) have introduced federal legislation[1] aimed at reining in the program. Sen. Cotton has called PACE "a scam."[2]

2. **PACE Loans Are Given First-Lien Status Over Mortgages.**
When a PACE program is used and a municipal bond issued, a tax lien is placed on the property. This lien has "super-priority," meaning that if there is a foreclosure, the PACE loan provider has to be paid back before other priority lien-holders, like mortgage providers. Legally, PACE programs do not have to notify the other priority lien-holders about the super-priority status.

---

[1] Protecting Americans from Credit Entanglements (PACE) Act of 2017, S. 838, https://www.congress.gov/bill/115th-congress/senate-bill/838/all-info

[2] Press Release, April 5, 2017, Office of Senator Tom Cotton, https://www.cotton.senate.gov/?p=press_release&id=653

3. **Mortgage Giants Fannie And Freddie Do Not Back Loans Associated with PACE.**
   Because the PACE loan is given first-lien status and is tied to the property itself, resulting in a tax lien, the loans represent an "unusual and difficult risk management challenges," according to the Federal Housing Finance Agency. [3] This is why the mortgage giants refuse to back most loans associated with the program, making it more difficult to sell a home with outstanding PACE obligations and creating potential out-of-pocket expenses for buyers who take on PACE-affiliated home purchases.

4. **PACE Financing Relies on and Distorts the Tax Code.**
   Instead of paying the lenders directly like in a traditional loan, loans are repaid through a higher annual assessment on property tax bills. The loan is attached to the property itself, distorting the tax code for the payment of personal and private loan obligations. The IRS even permits the interest portion of local PACE property tax payments to be deducted from personal income taxes, a benefit not always enjoyed by private loans that would achieve the same home upgrade outcome.[4]

5. **PACE Fast-Tracks Alternative Energy Mandates and Subsidies.**
   PACE loans can be used for a wide range of property upgrades, ranging from HVAC systems to solar panels. PACE loans don't require credit-checks and make it easier for a property owners to qualify for high interest loans for energy systems that are highly subsidized by taxpayers nationally. Additionally, through solar "net metering" policies and other generous tax credits, many of the upgrades being financed by local governments are those that take advantage of crony capitalism in the energy market. PACE exacerbates the problems inherent in alternative energy systems.

For more information on PACE, contact Paul Blair at pblair@atr.org.

---

[3] FHFA statement, July 2010 cited in LA Times. http://latimesblogs.latimes.com/money_co/2010/07/fannie-freddie-freeze-pace-energyefficiency-retrofit-financing-programs.html

[4] IRS Guidance Topic 503 – Deductible Taxes, June 20, 2016 http://pacenation.us/irs-says-pace-interest-falls-mortgage-deductibility-guidelines/