

Working draft for review and comment

Ohio Residential PACE Program Analysis and Recommendations

**Vacant and Abandoned Property Action Council (VAPAC)
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Executive Summary

Property Assessed Clean Energy (PACE) loans are a U.S. Department of Energy (DOE) designed program that enables property owners to borrow funds to make energy efficient property improvements by adding the costs to their property tax bill. The PACE program, which is implemented at the state and local government level, was first offered in northeast Ohio in 2010 as a financing tool for owners of commercial property. There is a general local consensus that this commercial program has been effective. PACE is now being proposed for residential property in Cuyahoga County. Funding for residential PACE in Ohio will be provided by bonds issued by the Lucas County Port Authority and loans that will be made by Renovate America, a private company that specializes in home improvement financing. ***The loans will be marketed directly to homeowners by contractors selling energy efficient home improvements*** (windows, furnaces, solar installations, etc.)

The Vacant and Abandoned Property Action Council (VAPAC), formed in 2005, focuses on abandonment and housing market destabilization caused by a variety of factors, including predatory loan practices. VAPAC's Tax Working Group has reviewed the proposed PACE program for Ohio, reviewed the program's history in other states, and reviewed the consumer protections being proposed for the program in Ohio. We find the proposed program poses significant risks to consumers, particularly in communities that are still struggling to recover from the past abuses of the foreclosure crisis. We find the proposed consumer protections to be insufficient to protect consumers.

Without significant changes in consumer protections, Residential PACE should not move forward in Northeast Ohio.

In the currently proposed form, Residential PACE is likely to have adverse outcomes, especially in vulnerable communities that only recently have begun to rebound from the foreclosure crisis. The proposed Ohio protections lack enforceability and do not go far enough to protect consumers.

PACE program lending is secured by a super-priority property tax lien that places a property at significant risk of loss in the event of default. No product that results in such a lien should be undertaken without significant consumer protections in place to minimize adverse outcomes. PACE loans that default also place a special burden on county and local governments who must then foreclose and manage the consequences of monitoring and addressing the condition of the resulting vacant properties. This places local governmental entities in the position of being a loan servicer.

We recognize that the need for home repair financing in the region is great. Strong advocacy efforts are needed to ensure that residents have access to credit, grants, and other tools to maintain their homes and undertake essential repairs. Residential PACE is proposed as a way for residents to access this much-needed financing in order to undertake energy efficiency improvements to their homes and realize resultant savings. But, as proposed, the program does not include measures to ensure homeowners actually benefit from these improvements such as energy audits or independent third-party (such as a local non-profit housing counseling agency) assessments of the scope of work. As a largely contractor-marketed program, there is significant risk that homeowners will be over-sold repairs that may not be in their best interest nor affordable. With an eight percent (8%) interest loan that could directly result in the foreclosure of a family's home, we can and must provide safeguards in the process, even if those safeguards make the program less profitable to the entities proposing it.

It is also worth asking whether the use of a government agency's bonding power could be put to better use in a non-profit managed loan-loss reserve program. Such a program could assist homeowners, who may not be eligible for other types of traditional financing, to make critical home repairs. Using the bonding power in the public interest in this way could address the challenge faced currently by local governments and non-profits, who have meager resources to help with home repair financing, yet have much expertise in running programs with proven track records of success.

Even if all of the proposed safeguards are implemented, it is our recommendation that Residential PACE be approached with extreme caution and consumers be advised and urged to consider other, less expensive and less risky financing tools for home repair.

General Overview and Findings

Local Commercial PACE Program is Effective and Established

In 2010, the First Suburbs Development Corporation assisted in the establishment of the Northeast Ohio Advanced Energy District (AED) to provide a commercial PACE program. Twenty communities are currently members of this AED, including the City of Cleveland. When a community passes enabling legislation to become a member of the AED, any commercial or industrial properties located in that municipality are able to apply for the financing for eligible projects. The AED was established as a tool to allow commercial and industrial property owners to make energy efficiency improvements without large out-of-pocket expenses. The AED allows these improvements to be assessed to the property tax duplicate over a period of up to 20 years. Many large and noteworthy projects have been completed and continue to be brought forward. It's clear that the AED has been and continues to be a successful economic development program for the region.

Residential PACE is being proposed for Ohio

In 2019, the Toledo Port entered into an Ohio HERO (Home Energy Renovation Opportunity) Program Administration Agreement with Renovate America, Inc.

Under the Renovate America Administration Agreement, the Toledo Port and Renovate America have agreed to establish and operate the Ohio HERO Program. The Ohio HERO Program will enable the owners of residential property in Ohio to use property assessed clean energy (PACE) financing to pay for energy efficiency and renewable energy improvements to their properties.

Often proposed as an alternative to credit card financing, a key distinction and source of concern of Residential PACE financing is that ownership of the property (in most cases the borrower's biggest asset) is at risk. Just as with the AED, the cost of the repairs or improvements will be assessed to the property tax duplicate as a super-priority lien, superseding any other liens including mortgage debt.

The Lucas County Port launched a successful pilot program, which was administered by the Lucas County Land Bank. The Land Bank provided technical assistance and final inspection of the installed improvements to homeowners. A 4.25 percent interest rate was charged on the loan. This differs from what will occur during a full-state roll-out, which will be administered by Renovate America and marketed through participating contractors, and would have an interest rate of 8 percent. The Land Bank's pilot program provided significant assistance to homeowners in determining the renovation needed and obtaining bids from reputable contractors. Without this type of non-profit assistance, the risks to a homeowner increase substantially. The lack of administration and oversight by a disinterested public agency creates the possibility of violations of consumer protection laws and best practices.

California, Florida, and Missouri currently have launched statewide Residential PACE programs. Undeniably, these programs have been popular. 220,000 homes have made repairs using the funding, with \$5.1 billion in improvements having been made.

Locally, the First Suburbs Consortium is working with Renovate America and their legal counsel, Bricker and Eckler, to bring Residential PACE to Northeast Ohio beginning with the NEO First Suburbs communities. As with the AED, cities that wish to participate must pass enabling legislation.

A cautionary tale in other states

Residential PACE programs, including those administered by Renovate America, have a problematic track record when it comes to consumer protection. The National Consumer Law Center has submitted extensive comments to the Consumer Financial Protection Bureau (CFPB) regarding Residential Pace consumer protection concerns. Their testimony includes several dozen case studies of consumers who were sold improvements that did not create the energy efficiency improvements promised; sold repairs or improvements that may not have been needed, and may not have been affordable to the homeowner. Since the costs are assessed as a super-priority property tax lien, this can result in the loss of consumers' homes through tax foreclosure. There is also legitimate criticism that the negative fallout from Residential PACE financing has a disparate impact on low income areas, communities of color, and elderly

homeowners. The marketing of Residential PACE financing tends to be largely contractor-driven, so there are legitimate concerns that contractors will over-sell unneeded products to consumers ***who are told they can receive the repairs with no out of pocket costs***. Typical repairs performed under Residential PACE financing include: HVAC, solar, roofing, windows and doors, and water efficiency projects.

In addition to the many homeowners facing payment problems and foreclosure after having taken out PACE loans, lawsuits have been filed in states with Residential PACE, including class action lawsuits filed in the State of California against Renovate America and Renew Financial, another PACE financing provider. Some [lawsuits](#) claim that Renew Financial, Renovate America and Los Angeles County “have spread a plague on thousands of low-income, elderly, and non-native English-speaking homeowners”, and include a claim for financial elder abuse.

A useful tool or a plague on homeowners?

Given the high average age of homes in Cuyahoga County and the difficulty many residents have in obtaining home repair and home improvement lending, having another tool in the tool box to encourage home repair is an attractive proposition. However, without thoughtfully considered and well-crafted consumer protections that can be effectively enforced, Residential PACE could further destabilize the region’s housing stock. After weathering and finally beginning to recover from the foreclosure crisis, Cuyahoga’s housing stock remains vulnerable. With over 30,000 units of tax delinquent parcels in the county and the capacity to foreclose on approximately 4,000 units per year, there remains a significant backlog of tax delinquent parcels. Creating a tool that could potentially add to this overwhelming problem and further destabilize a housing stock that is just beginning to recover, should be approached with extreme caution.

Ohio Consumer Protections are being proposed

To address negative publicity from other states, Renovate America is proposing special protections for Ohio consumers. The five pages of protections detailed by Renovate America focus on the following areas: Property Eligibility, Property Owner Eligibility, Improvement Eligibility, Disclosures and Documentation, Property Owner Support, Marketing and Communications, Contractor Requirements, Reporting, and Closing and Funding. Members of the VAPAC Delinquent Tax Working Group have had extensive conversations with Steve Sharpe from the National Consumer Law Center, have participated in a webinar from Renovate America, have spoken to Renovate America staff, and attended a session on Residential PACE at the 2019 Ohio Land Bank Conference, analyzed the testimony proposed by NCLC to the CFBP, reviewed national press coverage and analyzed enabling documentation including the Ohio Residential Pace Cooperative Agreement.

Are the Consumer Protections Enforceable and Effective?

The most pressing concern related to the proposed consumer protections is the lack of clarity regarding enforcement. Many of the proposed protections lack a defined mechanism for enforcement. Without consistent oversight and enforcement, the protections are meaningless.

Northeast Ohio has an established network of HUD approved non-profit housing counseling agencies. These agencies could play a key role in the application and approval process for Residential PACE to ensure that consumers can afford and truly need the proposed repairs, and to help identify if another, more desirable, funding source is available. Budget counseling could be a required component of the application process. Without that level of protective framework built in to the approval process, many concerns remain. It would be a prudent approach to have an entity performing an oversight role that does not have a financial interest in the project moving forward. As currently proposed, Renovate America, and the Lucas County Port have the primary roles in approving projects and both stand to profit when loans are made, with Renovate America, a for-profit company, receiving the bulk of the profits.

Core Concerns

1. Property Eligibility

There is no requirement for an energy audit that could show the cost-benefit analysis of the proposed repairs. Critics have often stated that exaggerated claims have been made on the energy savings from proposed repairs, and because repairs are financed for up to 20 years on the tax duplicate, some contractors have been accused of gouging customers on the total project cost. Could a homeowner be paying for the improvement after its useful life has expired? An energy audit by a professional certified by the DOE's National Renewable Energy Laboratory (NREL)¹, combined with technical assistance from a HUD-approved agency, could insure that a homeowner is making an informed decision, and not ignoring other, more critical repairs that should be completed before PACE-eligible, energy efficiency improvements should be undertaken.

Loan to value ratio is not clearly explained in the program proposal. How is the property appraised? Is Renovate America using the County assessed value – which could be out of date since the county only does a full appraisal every 6 years – or are they actually reviewing the property condition and area comparable sales? What process is in place to determine whether there are pending assessments that have not yet been placed on the tax duplicate at the time the PACE loan is originated? Property tax assessments are made once a year in Cuyahoga County, and finding pending assessments is complicated and may require a call to a municipality's Finance department.

2. Property Owner Eligibility and Underwriting

In response to the problems experienced in California with residential PACE, the California state legislature amended the California Financial Code to substantially increase consumer protections. Section 22687 of the California Financial Code now explicitly requires **third party verification** of a property owner's ability to repay a home improvement loan. Section 22687 provides a detailed list of acceptable forms of verification documents. In recognition of the problems experienced in California, the master cooperative agreement entered into by the Toledo-Lucas Port Authority, Renovate America, the Northeast Ohio Advanced Energy District and other energy districts, requires that consumer protections be adopted. Section 11 of the

¹ <https://www.energy.gov/eere/wipo/guidelines-home-energy-professionals-certifications>

agreement says ***“the consumer protection standards shall be substantively similar to the consumer protection standards adopted by the State of California for residential PACE”***.

However, the consumer protections proposed by Renovate America are not in compliance with the cooperative agreement. They say a homeowner may simply “attest” to their income, with ***no third party verification of ability to repay the loan***. This is no different than the requirements of the predatory “liar’s loans” and “no doc loans” that were prevalent during the mortgage foreclosure crisis. Tangible proof of income documents – substantively similar to what is required in California - should be required and verified before a loan can be originated.

In addition, debt to income ratio (DTI) does not specify front end (which ONLY includes mortgage debt) or back end DTI (which includes mortgage and all other debts). This distinction makes a critical difference in terms of calculating true affordability). Lack of details and specific requirements may mean there are no teeth in this aspect of the consumer protections.

3. Disclosures and Documentation

There is an overall lack of clarity related to repayment. Some questions remain such as:

- How are interest rates and fees calculated?
- Do they represent a premium over traditional financing?
- How are principal and interest allocated in repayment?
- Is the indebtedness paid in equal installments or would the interest be paid before the principal?
- What happens in the event of a default?
- Are the consumer protections proposed by Renovate America merely suggested policies, or are they enforceable standards?
- Who would have the power to enforce violations of consumer protections?
- How will subsequent sales of the property be affected by the presence of a PACE loan?

4. Property Owner Support

What recourse is available to a consumer if the project goes bad after the loan is signed off on and the project initially approved? Some defects cannot be determined in an initial city inspection and may not be found until months or years later. What if a contractor walks off a job before it is completed? How are those situations handled? Even if the loan is not closed or the contractor not paid, what can be done to assist the property owner? Who is responsible for providing the assistance? Homeowners using PACE financing may not have the resources to undertake expensive legal action against contractors.

5. Marketing and Communications

Residential PACE is essentially a contractor-marketed program. At the point of sale (often in the living room of a prospect), the contractor proactively offers PACE as a “no money down” way to get the project completed. Because it appears to be a “government sponsored” program, consumers may be lulled into thinking they are entering into a “safe” contract, and may not be fully aware of the risk they are taking on with their home. Even with a telephone disclosure session on a recorded line, these consumers should be given an adequate cancellation period to read through the disclosures, and, more importantly, be provided

assistance from a non-profit counseling agency to review other possible home repair and funding options before committing to a PACE loan. There is an inherent risk that because of the length of the payment contract and the delayed payback that consumers may be inclined to make larger improvements than they need or can afford, or perhaps ignore other critical home repairs that may not be eligible for PACE financing that would be prudent to complete before energy efficiency improvements are made. There need to be proper disclosures given to homeowners and rules in place to prevent “up-selling” and over-promising on the energy savings of repairs.

6. Contractor Requirements

Contractor monitoring is not clearly specified. California has more clear definitions and specific requirements, and is proposing expansive regulations. No such detail is being provided for Ohio. Once a project has been approved and completed, how are contractor complaints handled if the project later proves to be poorly completed? Renovate asks municipalities to recommend contractors to participate in the program, however most cities cannot endorse or recommend contractors.

What are the standards for certifying contractors to participate in and market the program?

Who ensures that permits are being pulled?

Will funds be available to compensate a homeowner for contractor-related property damage?

7. Reporting

A flow chart or diagram that clearly explains the specific and detailed roles and responsibilities related to these loans and corresponding record-keeping is needed. The flow chart should define the roles of cities, the county, Renovate, the Lucas County Port, etc. This will help determine the amount of time various entities will need to potentially spend administering the program.

8. Closing and Funding

PACE funding is essentially a home improvement contractor mortgage loan. As a super-priority lien, there is little to no risk for the entity making the loan. Renovate America states that they have a zero-default rate on Residential PACE loans, but defaults will occur perhaps years later, as the consumers find themselves in property tax delinquency and the County Prosecutor ends up being the collection agent through the tax foreclosure process. Currently, the capacity to file tax foreclosures is limited to less than 4,000 cases a year, with over 30,000 delinquent parcels existing currently. Mortgage foreclosures are also a possible result of PACE loans, as escrow payments balloon to levels that may not be affordable as a result of the tax assessment. Although it is difficult to tie PACE loans directly to these defaults, PACE provider claims of a “zero default rate” should be approached with some skepticism.

Funding to help with the back-end collection process, i.e. the county prosecutor, is not built into this program. In fact, the Residential Pace program offers no funding support to municipalities, county government, or foreclosure counseling agencies, even though these

entities will have a significant role to play in implementing the program and addressing any issues downstream.

Recommendations

1. Provide enhanced and well-defined consumer protections with a clearly specified method of enforcement, including enforcement directly by the homeowner, and penalties for non-compliance.
2. Designate a single local entity to provide oversight and monitoring, that is independent and has no financial interest in loans being made through the Residential PACE program.
3. Require a free energy audit by an independent professional (not the contractor) that has a DOE-NREL-compliant certification. The audit shall include a written report with specific requirements for energy improvements. The report must be provided to the homeowner prior to entering into a PACE financing contract.
4. Fund HUD-approved housing counseling agencies to assist homeowners in the following ways:
 - a. Counsel homeowners during a pre-application process: assess, identify and recommend needed repairs and improvements for the home to maximize health, safety and property value as well as the property owner's financial ability to pay.
 - b. Review the loan application and the home improvement contract with the homeowner.
 - c. Inspect the work at appropriate stages and certify that the work has been completed satisfactorily. This should be done in addition to any municipal inspection.
5. Loan approval must include the following underwriting requirements:
 - a. Third party verification of income substantively similar to what is specified by the State of California, as required in the master cooperative PACE agreement with the Toledo-Lucas Port Authority.
 - b. Debt to income (DTI) ratio based on mortgages and all other debts (back end DTI)
 - c. Loan to value (LTV) ratio based on property inspection and recent comparable property sales.
 - d. Certification from the local municipality that there are no pending assessments that have not yet been attached to the tax duplicate.
6. Consumer financial and repayment disclosures must be clear, detailed, and easy-to-understand. It should be made very clear that the property is being placed at risk of foreclosure if the debt is not repaid.
7. Establish clearly defined standards for certifying contractors and penalties for compliance infractions. Prohibit "up-selling" by contractors.
8. Provide a clearly defined process to assist Property owners with complaints against contractors.
9. The contract should specifically provide for a cancellation period, as follows:²

² Ohio Revised Code Section 1345.22.

- a. **“The buyer/homeowner has the right to cancel this contract until midnight of the third business day after the day on which this contract is signed. Cancellation shall be in writing and delivered to the seller/contractor’s physical address, email address or fax number stated in the contract.”**
 - b. **“The seller/contractor shall not begin the work described in the contract during the cancellation period described above.”**
 - c. **“Any loan or other indebtedness associated with the contract shall not close during the cancellation period described above.”**
 - d. The above language in a, b and c shall be prominently displayed in the contract and in any promissory note or loan document the homeowner signs.
 - e. The cancellation period described above shall not apply if all of the following apply:
 - i. The homeowner initiates the contact with the seller/contractor,
 - ii. The services described in the contract are needed to meet a bonafide immediate personal emergency of the homeowner which will jeopardize the welfare, health, or safety of natural persons, or endanger property which the homeowner owns, and
 - iii. The homeowner gives the seller/contractor a separate, dated and signed statement in the buyer’s handwriting that:
 - 1) describes the situation requiring immediate remedy and
 - 2) expressly acknowledges and waives the right to cancel as described above.
10. Define a process to ensure that required building permits and inspections have occurred.
 11. Provide a flow chart that outlines the timing and the process for a typical transaction and the roles of all parties involved in contracting, financing, oversight, assessments, and enforcement.
 12. Provide funding support to help cover the costs of all of the parties that play a role in implementation and oversight (municipalities, county government, and housing counseling agencies) that does not require an additional cost to be added to the loan.
 13. Commit to providing quarterly and annual metrics and statistics, detailing the properties served by PACE loans, the scope of work, cost of the project, and the contractor doing the work. Obtain an annual third-party evaluation of results, so that the success of the program can be tracked over time and the program adjusted to minimize adverse outcomes. Cleveland State University has provided this type of analysis for years related to the outcomes of local, non-profit foreclosure counseling agencies.

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