



City Council Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL **DATE:** July 27, 2010
FROM: PUBLIC UTILITIES DEPARTMENT **ITEM NO:** 36
WARDS: ALL
SUBJECT: CITY OF RIVERSIDE ENERGY HIGH EFFICIENCY LOAN PROGRAM (E-HELP)

ISSUE:

The suspension of certain Energy High Efficiency Loan Program (E-HELP) activities in accordance with the Federal Housing Finance Agency's (FHFA) Statement and the Office of the Comptroller of the Currency's Bulletin.

RECOMMENDATIONS:

That the City Council:

1. Adopt a resolution ordering certain actions regarding the Energy High Efficiency Loan Program;
2. Direct staff to suspend acceptance of applications from and the provision of financing for the E-HELP program from residential and commercial City of Riverside property owners so as long as the Federal Housing Finance Agency's (FHFA) Statement and the Office of the Comptroller of the Currency's Bulletin are in effect; and
3. Direct staff to prepare a letter on behalf of the Mayor setting for the City's position and asking for appropriate federal legislation to allow the E-Help Program to continue.

BACKGROUND:

On July 21, 2008, Assembly Bill (AB) 811 was signed into law. Essentially, the program allowed cities to loan money to customers for energy efficiency improvements at their homes or facilities and repay the loan over time through their property tax bills. Specifically, the bill authorized cities to establish a program to enter into contractual assessment agreements with property owners to finance the installation of distributed generation, energy efficiency improvements, and renewable energy sources that are permanently fixed to real property. Once established, the cities could provide a loan to property owners for the purchase and installation of such improvements. Property owners would then repay the loan through a contractual assessment on their property. The contractual assessments are collected on property owner's tax bills at the same time and in the same manner as property taxes. As with all property-related assessments, the loan would have a super-priority lien over all existing mortgages. Such programs have been adopted nationwide, and are generally known as Property Assessed Clean Energy ("PACE") programs.

On May 25, 2010, the City Council adopted a resolution forming a Sustainable Energy Financing District to provide financing to City property owners for the installation of energy efficiency improvements to their homes and businesses. Since this time, the City has not accepted any applications for the E-HELP program, nor has any property owner within the City been provided with such special financing. The program had gone through the entire approval process, including three public hearings, and Riverside Public Utilities (RPU) was just about to begin accepting loan applications. (The E-Help program is a PACE-like program.)

Fannie Mae and Freddie Mac did not support the lien structure where the E-HELP loan repayments receive priority over repayment of other mortgages on the property. These two agencies purchase home loans from banks and other lenders, so as to allow banks to free up more capital for additional home mortgage lending. Given the current economic conditions, Fannie Mae and Freddie Mac have been purchasing a significant amount of mortgages. If a lender issues a mortgage that does not meet the requirements or standards of Fannie Mae and Freddie Mac, the lender may be unable to sell the mortgage to these entities. In effect, Fannie Mae and Freddie Mac now have a significant amount of control over the local mortgage market. Fannie Mae and Freddie Mac have expressed concern about the priority position that these energy efficiency loans would have over mortgages and have directed that all PACE-like loans (and the super priority of the loan) must be approved by the mortgage holder prior to their issuance.

Fannie Mae and Freddie Mac are regulated by the federal government. On July 6, 2010, the Federal Housing Finance Agency ("FHFA") issued a statement and the Office of the Comptroller of the Currency ("OCC") issued a bulletin. The FHFA and the OCC determined that certain energy retrofit lending programs present significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac and the Federal Home Loan Banks for PACE programs. In effect, these two directives ordered Fannie Mae and Freddie Mac to require that all PACE loans be approved by the mortgage holder. This also means that Fannie Mae and Freddie Mac will not purchase any mortgages with unapproved PACE loans, and banks may be reluctant to make a loan in a jurisdiction that has a PACE program. The directives also raise serious concerns for PACE participants who are trying to refinance their houses.

On July 14, 2010, the California Attorney General sued the federal government in an attempt to alter the directive issued by the FHFA. In that complaint, the Attorney General noted that several jurisdictions, including San Francisco and Placer County, have suspended their programs and that as of the date of the complaint, 22 participants in Sonoma County's PACE program were unable to sell or refinance their property without paying off the PACE loan in full.

Accordingly, until this issue is resolved either through federal legislation or the Attorney General's lawsuit, the E-HELP PACE-loan program should be suspended, so as to not adversely impact homeowners in the City of Riverside. While RPU staff have created and evolved the E-HELP program right to the point of implementation, continuing with the E-HELP program would appear to have a very negative impact on the sale of real estate in Riverside. It is also not recommended that RPU consider loans with no real collateral from reserves due to repayment uncertainty.

FISCAL IMPACT:

There is no fiscal impact associated with this report.

Prepared by: David H. Wright, Public Utilities General Manager
Certified as to availability
of funds: Paul C. Sundeen, Assistant City Manager/CFO/Treasurer
Approved by: Belinda J. Graham, Assistant City Manager
for Bradley J. Hudson, City Manager
Approved as to form: Gregory P. Priamos, City Attorney

Attachments:

1. Resolution
2. FHFA Statement
3. OCC Bulletin

1 RESOLUTION NO.

2 A RESOLUTION OF THE CITY COUNCIL OF THE CITY OF RIVERSIDE,
3 CALIFORNIA ORDERING CERTAIN ACTIONS REGARDING THE ENERGY HIGH
4 EFFICIENCY LOAN PROGRAM

5 WHEREAS, the City has established a program entitled the Energy High Efficiency Loan
6 Program ("E-HELP program") to provide financing for the installation of energy efficiency
7 improvements, including but not limited to solar installations, for residential and commercial
8 customers of the City's Electric Utility; and

9 WHEREAS, on May 25, 2010, as part of the E-HELP program, the City Council adopted a
10 resolution forming a Sustainable Energy Financing District to provide financing for the installation
11 of energy efficiency improvements on property owners in the City; and

12 WHEREAS, the City has not accepted any applications for the E-HELP program, nor has any
13 property owner within the City been provided with such special financing; and

14 WHEREAS, on July 6, 2010, the Federal Housing Finance Agency issued the Statement
15 attached hereto as Exhibit A (the "Statement"); and

16 WHEREAS, also on July 6, 2010, the Office of the Comptroller of the Currency issued the
17 Bulletin attached hereto as Exhibit B (the "Bulletin"); and

18 WHEREAS, as a result of the Statement and the Bulletin and in order to avoid any adverse
19 impact on property owners in the City as a result of the E-HELP program, the City Council wishes to
20 declare that, as long as the Statement and the Bulletin are in effect, it will not accept applications for
21 the E-HELP program or provide financing through the E-HELP program to property owners in the
22 City.

23 NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Riverside,
24 California, as follows:

25 Section 1: Recitals Correct. The foregoing recitals are true and correct

26 Section 2: Termination of Certain E-Help Program Activities. The City Council hereby
27 orders that, as long as the Statement and the Bulletin are in effect, the City shall not accept
28 applications for the E-HELP program or provide financing through the E-HELP program to property

1 owners in the City. The City Council hereby orders that, except as provided in the previous
2 sentence, the E-HELP program shall remain in full force and effect.

3 Section 3: Effective Date. This resolution shall take effect upon its adoption.

4
5 ADOPTED by the City Council this _____ day of _____, 2010.

6
7
8 RONALD O. LOVERIDGE
Mayor of the City of Riverside

9 Attest:

10
11 COLLEEN J. NICOL
City Clerk of the City of Riverside

12
13 I, Colleen J. Nicol, City Clerk of the City of Riverside, California, hereby certify that the
14 foregoing resolution was duly and regularly adopted at a meeting of the City Council of said City at
15 its meeting held on the _____ day of _____, 2010, by the following vote, to wit:

16 Ayes:

17 Noes:

18 Absent:

19 Abstain:

20
21 IN WITNESS WHEREOF, I have hereunto set my hand and affixed the official seal of the
22 City of Riverside, California, this _____ day of _____, 2010.

23
24 COLLEEN J. NICOL
City Clerk of the City of Riverside

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26 O:\Cycom\WPDocs\D020\P010\00043194.DOC
27 07-2770.2 sw 07/20/10

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36-5

FEDERAL HOUSING FINANCE AGENCY



STATEMENT

For Immediate Release
July 6, 2010

Contact: Corinne Russell (202) 414-6921
Stefanie Mullin (202) 414-6376

FHFA Statement on Certain Energy Retrofit Loan Programs

After careful review and over a year of working with federal and state government agencies, the Federal Housing Finance Agency (FHFA) has determined that certain energy retrofit lending programs present significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac and the Federal Home Loan Banks. Specifically, programs denominated as Property Assessed Clean Energy (PACE) seek to foster lending for retrofits of residential or commercial properties through a county or city's tax assessment regime. Under most of these programs, such loans acquire a priority lien over existing mortgages, though certain states have chosen not to adopt such priority positions for their loans.

First liens established by PACE loans are unlike routine tax assessments and pose unusual and difficult risk management challenges for lenders, servicers and mortgage securities investors. The size and duration of PACE loans exceed typical local tax programs and do not have the traditional community benefits associated with taxing initiatives.

FHFA urged state and local governments to reconsider these programs and continues to call for a pause in such programs so concerns can be addressed. First liens for such loans represent a key alteration of traditional mortgage lending practice. They present significant risk to lenders and secondary market entities, may alter valuations for mortgage-backed securities and are not essential for successful programs to spur energy conservation.

While the first lien position offered in most PACE programs minimizes credit risk for investors funding the programs, it alters traditional lending priorities. Underwriting for PACE programs results in collateral-based lending rather than lending based upon ability-to-pay, the absence of Truth-in-Lending Act and other consumer protections, and uncertainty as to whether the home improvements actually produce meaningful reductions in energy consumption.

Efforts are just underway to develop underwriting and consumer protection standards as well as energy retrofit standards that are critical for homeowners and lenders to understand the risks and rewards of any energy retrofit lending program. However, first liens that disrupt a fragile housing finance market and long-standing lending priorities, the absence of robust underwriting standards to protect homeowners and the lack of energy retrofit standards to assist homeowners, appraisers, inspectors and lenders determine the value of retrofit products combine to raise safety and soundness concerns.

On May 5, 2010, Fannie Mae and Freddie Mac alerted their seller-servicers to gain an understanding of whether there are existing or prospective PACE or PACE-like programs in jurisdictions where they do business, to be aware that programs with first liens run contrary to the Fannie Mae-Freddie Mac Uniform Security Instrument and that the Enterprises would provide additional guidance should the programs move beyond the experimental stage. Those lender letters remain in effect.

Today, FHFA is directing Fannie Mae, Freddie Mac and the Federal Home Loan Banks to undertake the following prudential actions:

1. For any homeowner who obtained a PACE or PACE-like loan with a priority first lien prior to this date, FHFA is directing Fannie Mae and Freddie Mac to waive their Uniform Security Instrument prohibitions against such senior liens.
2. In addressing PACE programs with first liens, Fannie Mae and Freddie Mac should undertake actions that protect their safe and sound operations. These include, but are not limited to:
 - Adjusting loan-to-value ratios to reflect the maximum permissible PACE loan amount available to borrowers in PACE jurisdictions;
 - Ensuring that loan covenants require approval/consent for any PACE loan;
 - Tightening borrower debt-to-income ratios to account for additional obligations associated with possible future PACE loans;
 - Ensuring that mortgages on properties in a jurisdiction offering PACE-like programs satisfy all applicable federal and state lending regulations and guidance.

Fannie Mae and Freddie Mac should issue additional guidance as needed.

3. The Federal Home Loan Banks are directed to review their collateral policies in order to assure that pledged collateral is not adversely affected by energy retrofit programs that include first liens.

Nothing in this Statement affects the normal underwriting programs of the regulated entities or their dealings with PACE programs that do not have a senior lien priority. Further, nothing in these directions to the regulated entities affects in any way underwriting related to traditional tax programs, but is focused solely on senior lien PACE lending initiatives.

FHFA recognizes that PACE and PACE-like programs pose additional lending challenges, but also represent serious efforts to reduce energy consumption. FHFA remains committed to working with federal, state, and local government agencies to develop and implement energy retrofit lending programs with appropriate underwriting guidelines and consumer protection standards. FHFA will also continue to encourage the establishment of energy efficiency standards to support such programs.

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The Federal Housing Finance Agency regulates Fannie Mae, Freddie Mac and the 12 Federal Home Loan Banks. These government-sponsored enterprises provide more than \$5.9 trillion in funding for the U.S. mortgage markets and financial institutions.

**OCC 2010-25**
OCC BULLETIN

Comptroller of the Currency
Administrator of National Banks

Subject: **Property Assessed Clean
Energy (PACE) Programs**

Description: **Supervisory Guidance**

Date: July 6, 2010

TO: Chief Executive Officers of All National Banks, Department and Division Heads,
and All Examining Personnel

The Office of the Comptroller of the Currency (OCC) is issuing this guidance to alert national banks to concerns and regulatory expectations regarding certain state and local lending programs for energy retrofitting of residential and commercial properties, frequently termed a Property Assessed Clean Energy (PACE) program. PACE or PACE-like (PACE) programs use the municipal tax assessment process to ensure repayment. Under most of these programs, such loans acquire priority lien, thereby moving the funds advanced for energy improvements ahead of existing first and subordinate mortgage liens.¹ This lien infringement raises significant safety and soundness concerns that mortgage lenders and investors must consider. Reflecting these concerns, the Federal Housing Finance Agency (FHFA) today issued the attached statement directing actions that Fannie Mae, Freddie Mac, and the Federal Home Loan Banks should undertake to protect their operations with regards to such programs.

National banks need to be aware of the FHFA's directives for loans that they may originate with the intent to sell to the government sponsored entities. More generally, national banks should ascertain if such programs exist in jurisdictions where they do business, determine whether those programs alter banks' lien positions, and carefully consider the programs' impact on both banks' current mortgage portfolios and ongoing mortgage lending activities.

National bank lenders should take steps to mitigate exposures and protect collateral positions. For existing mortgage and home equity loans, actions may include the following in accordance with applicable law:

- Procuring loss guarantees from the respective states or municipalities;
- Escrowing tax assessment-related debt service payments;
- Re-evaluating and adjusting home equity line of credit (HELOC) line amounts; and
- In the case of commercial properties, securing additional collateral.

For new mortgage and home equity loans, mitigating steps may include:

- Reducing real estate loan-to-value limits to reflect maximum advance rates of PACE programs to the extent they create super-senior lien priorities; and
- Considering the maximum amount of the PACE payment portion of the annual tax assessment in the institution's analysis of the borrower's financial capacity.

In addition, banks that invest in mortgage backed securities or that are considering the purchase of pools of mortgage loans should consider the impact of tax-assessed energy advances on their asset valuations. Finally, the OCC expects investment banking units to be cognizant of the impact of this type of funding vehicle on their respective institutions and on the mortgage market overall when making any decisions regarding associated bond underwriting.

The OCC supports commercial and residential energy lending when such lending programs observe existing lien preference, ensure prudent underwriting, and comply with appropriate consumer protections. Programs that fail to comply with these expectations pose significant regulatory and safety and soundness concerns.

For questions or further information, please contact Joseph A. Smith, Group Leader, Retail Credit Division at (202) 874-5170.

/signed/

Timothy W. Long
Senior Deputy Comptroller for Bank Supervision Policy
and Chief National Bank Examiner

Attachment: FHFA Statement
[<http://www.fhfa.gov/webfiles/15884/PACESTMT7610.pdf>]

¹ Some states have chosen not to adopt such priority positions for their loans.

For instructions on how to view attachments, visit the [Accessibility page](#).