July 19, 2016

Mortgagee Letter 2016-11

To
All FHA Approved Mortgagees
All Direct Endorsement Underwriters
All FHA Roster Appraisers
All FHA Roster Inspectors
All FHA Approved 203(k) Consultants
All HUD Approved Housing Counselors
All HUD Approved Nonprofit Organizations
All Governmental Entity Participants
All Real Estate Brokers
All Closing Agents

Subject
Property Assessed Clean Energy (PACE)

Purpose
This transmits updates to the following sections of HUD Handbook 4000.1, Single Family Policy Handbook:

- Section II.A.1.a.i(E)(1)(a)(iii), Sales Contract and Supporting Documentation
- Section II.A.1.a.iii(B)(6)(e), Additional Requirements When Ordering an Appraisal
- Section II.A.1.b.iv(A)(6), Property Assessed Clean Energy (PACE)
- Section II.A.4.a.iii(A)(1), Automated Underwriting System Data Entry Requirements
- Section II.A.4.d.iii(G)(2), Interested Party Contributions (TOTAL)
- Section II.A.5.c.iii(G)(2), Interested Party Contributions (Manual)
- Section II.A.5.d.vii(B), Calculating Total Mortgage Payment
- Section II.A.6.a.viii(A), Monthly Escrow Obligation
- Section IID.12.d.iv, Property Assessed Clean Energy (PACE)
Effective Date
These Handbook sections are effective for all case numbers assigned on or after 60 days from publication of this Mortgagee Letter; however, Mortgagees may begin using the policy immediately.

4000.1 FHA Single Family Housing Policy Handbook
The attached updates to HUD’s Single Family Housing Policy Handbook 4000.1 will be incorporated in a future publication of the Handbook.

Background
FHA supports the goals of clean energy, energy efficiency, and resilience. Property Assessed Clean Energy (PACE) programs may provide an alternative means of financing energy and other PACE-allowed improvements to residential properties using financing provided by private enterprises in conjunction with state and local governments.

The terms and conditions of the PACE obligation may vary by state, local government, and PACE program. PACE programs also determine the scope of allowable improvements made under their respective PACE programs. Generally, the repayment of the PACE obligation is collected in the same manner as a special assessment is collected by the local government, rather than paid directly by the Borrower to the party providing the PACE financing. Generally, the PACE obligation is also secured in the same manner as a special assessment against the property. In the event of the sale, including a foreclosure sale, of the property with outstanding PACE financing, the obligation will continue with the property causing the new homeowner to be responsible for the payments on the outstanding PACE amount. In cases of foreclosure, priority collection of delinquent payments for the PACE assessment may be waived or relinquished.

The Department of Energy is updating its Best Practices Guidelines for Residential PACE Financing, which may be used by states and counties to align with their consumer protection goals.

FHA regulations at 24 CFR §203.32(a) require, in part, that with certain exceptions, at the time the mortgage is offered for insurance, the property must be free and clear of any liens other than the FHA-insured mortgage. In addition, FHA regulations at 24 CFR §203.41(c)(2) require that any restrictions on conveyance automatically terminate if title to the mortgaged property is transferred by foreclosure or deed-in-lieu of foreclosure, or if the FHA-insured mortgage is assigned to the Secretary.

Continued on next page
Attached to this ML are additions and revisions to the Handbook 4000.1. The following is a summary of Title II Forward Mortgage policy changes, which is provided for informational purposes only.

**Outstanding PACE Obligations**

Properties which will remain encumbered with a PACE obligation may be eligible for FHA-insured mortgage financing, provided that the mortgagee determines that the following requirements have been met:

- under the laws of the state where the property is located, the PACE obligation is collected and secured by the creditor in the same manner as a special assessment against the property;
- the property may only become subject to an enforceable claim (i.e., a lien) that is superior to the FHA-insured mortgage for delinquent regularly scheduled PACE special assessment payments. The property shall not be subject to an enforceable claim (i.e., lien) superior to the FHA-insured mortgage for the full outstanding PACE obligation at any time (i.e., through acceleration of the full obligation.) However, a notice of lien for the full PACE obligation may be recorded in the land records;
- there are no terms or conditions that limit the transfer of the property to a new homeowner. Legal restrictions on conveyance arising from a PACE obligation that could require the consent of a third party before the owner can convey the real property are prohibited, unless such provisions may be terminated at the option of, and with no cost to, the homeowner;
- the existence of a PACE obligation on a property is readily apparent to mortgagees, appraisers, borrowers and other parties to an FHA-insured mortgage transaction in the public records and must show the obligation amount, the expiration date and cause of the expiration of the assessment, and in no case may default accelerate the expiration date; and
- in the event of the sale, including a foreclosure sale, of the property with outstanding PACE financing, the obligation will continue with the property causing the new homeowner to be responsible for the payments on the outstanding PACE amount.

**Disclosure of PACE Obligation, Terms and Conditions upon Sale**

For properties with existing PACE obligations, the property sales contract must indicate whether the obligation will remain with the property or be satisfied by the seller at, or prior to closing. Where the obligation will
remain, all terms and conditions of the PACE obligation must be fully disclosed to the borrower and made part of the sales contract between the seller and the borrower.

**Appraisal Requirements**

Where energy and other PACE-allowed improvements have been made to the property through a PACE program, and the PACE obligation will remain outstanding, the appraiser must analyze and report the impact on the value of the property, whether positive or negative, of the PACE-related improvements and any additional obligation (i.e., the PACE special assessment).

**Home Equity Conversion Mortgages and Title I Loans**

These policies are not applicable to Home Equity Conversion Mortgages (HECM) or Title I Loans. Properties with PACE obligations are not eligible for an FHA-insured HECM or Title I Loan.

**Information Collection**

The information collection requirements contained in this document have been approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501-3520) and assigned OMB control number 2502-0059 and OMB Control number 2502-0538. In accordance with the Paperwork Reduction Act, HUD may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

**Questions**

Please address any questions about the topics addressed in this Mortgagee Letter to the FHA Resource Center at (800) 225-5342. Persons with hearing or speech impairments may reach this number via TTY by calling the Federal Relay Service at (800) 877-8339. For additional information on this Mortgagee Letter, please visit www.hud.gov/answers.

**Signature**

Edward L. Golding  
Principal Deputy Assistant Secretary for Housing

**Attachments**

[1], [2], [3], [4], [5], [6], [7], [8], [9], [10]

(Download zip file)