



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

ASSISTANT SECRETARY FOR HOUSING –
FEDERAL HOUSING COMMISSIONER

Date: January 19, 2017

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 Government Entity Participants
All Real Estate Brokers
All Closing Agents

MORTGAGEE LETTER 2017-06

Subject	Servicing of FHA-insured Mortgages on Properties Encumbered with a Property Assessed Clean Energy (PACE) Obligation
Purpose	The purpose of this Mortgagee Letter is to provide policies and procedures for the servicing of FHA-insured mortgages on properties encumbered with a PACE obligation.
Effective Date	Policy revisions are effective immediately. All policy updates will be incorporated into a future publication of the HUD Single Family Housing Policy Handbook 4000.1 (Handbook 4000.1).
Affected Programs	This guidance applies to all FHA Title II forward mortgage programs.
Affected Topics	This guidance will affect Handbook 4000.1 sections III.A.1.e., <i>Payment Administration</i> ; III.A.1.g.ii., <i>Escrowing of Funds</i> ; III.A.2.1.ii., <i>Pre-foreclosure Sales</i> ; III.A.2.1.iii., <i>Deed-in-Lieu of Foreclosure</i> ; III.A.2.p., <i>Claims Without Conveyance of Title</i> ; III.A.2.r., <i>Foreclosure</i> ; III.A.2.t., <i>Conveyance of Acquired Properties</i> ; and III.A.3.b., <i>Assumptions</i> .
Background	Policies and requirements for Properties encumbered with a PACE obligation to be eligible for FHA-insured mortgage financing were announced in Mortgagee Letter 2016-11 and were subsequently incorporated into

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Handbook 4000.1, FHA Single Family Housing Policy Handbook, in the September 30, 2016 Handbook revision.

The terms and conditions of a PACE obligation may vary by state, local government, and PACE program. Generally, a PACE obligation is secured and collected in the same manner as a special assessment is treated by the local government; funds obligated are not paid directly by the Borrower to the party providing the PACE financing.

In the event of the sale, including a foreclosure sale, of a property with an 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.

This Mortgagee Letter transmits updates to the Servicing Section of the Handbook (Section III) to incorporate conforming revisions to escrow, appraisal and property conveyance requirements.

Summary of Changes

Changes to HUD Handbook 4000.1 affected topics are as follows:

- *Application of Payments* (section III.A.1.e.ii) has been modified to state that escrowed items include any assessments related to a PACE obligation.
- *Escrowing of Funds* (section III.A.1.g.ii) has been revised to include a new Paragraph (C) Items to be Escrowed. The existing Paragraph (C) Required Documentation is re-designated as Paragraph (D).
- *Pre-Foreclosure Sales* (section III.A.2.1.ii.) includes revised requirements to determine whether the title is impaired by a PACE obligation, analysis and reporting in the PFS appraisal of a PACE obligation that will remain outstanding, and disclosure of any PACE obligation in the property sales contract. Owner-Occupant Borrower Compensation may be used to resolve a PACE obligation.
- *Deed-in-Lieu of Foreclosure* (section III.A.2.1.iii.) has been revised to state that HUD will allow a notice of lien recorded in the land records to secure repayment of a PACE obligation that may only become subject to an enforceable claim (i.e., a lien) for delinquent regularly scheduled PACE special assessment payments and otherwise complies with the eligibility and acceptability criteria for Properties encumbered with a PACE obligation provided in Section II.A.1.b.iv.(A)(6). Owner-Occupant Borrower Compensation may be used to resolve a PACE obligation.
- *Claims Without Conveyance of Title* (section III.A.2.p.) includes a requirement for analysis and reporting in the CWCOT appraisal of an outstanding PACE obligation. The existing Paragraph (3) Required Documentation is re-designated as Paragraph (4).

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- *Foreclosure* (section III.A.2.r) has been modified to require a PACE obligation review.
- *Conveyance of Acquired Properties* (section III.A.2.t) has been revised to state that HUD will allow a notice of lien recorded in the land records to secure repayment of a PACE obligation that may only become subject to an enforceable claim (i.e., a lien) for delinquent regularly scheduled PACE special assessment payments and otherwise complies with the eligibility and acceptability criteria for Properties encumbered with a PACE obligation provided in Section II.A.1.b.iv.(A)(6). Prior to the conveyance of a Property to HUD, the Mortgagee must pay PACE assessments currently due and payable at the time of conveyance or within 30 Days of conveyance. Mortgagees must not satisfy the full PACE obligation and seek reimbursement of such funds as part of their FHA claim.
- *Assumptions* (section III.A.3.b) includes a revised requirement that the Mortgagee advise the selling Borrower that any existing PACE obligation that will remain with the property must be fully disclosed to the buyer and made part of the sales contract.

The abovementioned policy changes will be incorporated into Handbook 4000.1 and appear as follows:

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Application of Payments (III.A.1.e.ii.)

Mortgagees using special custodial accounts must withdraw an amount equal to the principal, interest, and service charges within 30 Days after deposit and post to the Borrower's records accordingly.

The Mortgagee must apply Borrower payments in the following order:

- to mortgage insurance premiums (MIPs) due, if any;
- to charges for ground rents, taxes, special assessments, including any assessments related to a PACE obligation, flood insurance premiums, if required, and fire and other hazard insurance premiums;
- to interest on the Mortgage;
- to amortization of the principal of the Mortgage; and
- to Late Charges, provided, that any amounts owed for Late Charges must be handled consistent with TILA regulations.

The Mortgagee may only apply funds for payments of optional insurance coverage premiums after the application of funds to all other elements of the monthly Mortgage Payment.

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Escrowing of Funds – Items to be Escrowed (III.A.1.g.ii.(C))

The Mortgagee must require that the total Borrower Mortgage Payment includes escrow funds to provide for payment of property charges in accordance with 24 CFR § 203.23, the security instrument, and applicable law. Items to be escrowed include:

- real estate taxes;
- special assessments, including any assessments related to a PACE obligation;
- hazard insurance required by the Mortgagee;
- flood insurance as applicable;
- FHA Mortgage Insurance Premium;
- Ground Rent, if any;
- other items which can attain priority over the Security Instrument as a lien or encumbrance on the Property, other than condominium or Homeowners' Association (HOA) fees.

Escrowing of Funds – Required Documentation (III.A.1.g.ii.(D))

The Mortgagee must retain documentation of its holding of all escrow funds on deposit.

Pre-Foreclosure Sales – Eligibility – Condition of Title (III.A.2.1.ii.(B)(4))

The Mortgagee must ensure that all FHA-insured mortgaged Properties sold under the PFS Program have clear marketable title.

Before approving a Borrower for participation in the PFS program, the Mortgagee must obtain a title search or preliminary report and determine whether the title is impaired by:

- unresolvable title problems;
- liens that cannot be discharged as permitted by HUD; or
- a PACE obligation.

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Pre-Foreclosure Sales – Disclosure Requirements for PFS Transactions (III.A.2.1.ii.(C)(2))

Before approving the Borrower for the PFS Option, the Mortgagee must notify the Borrower in writing of the following:

- The Mortgage must be in Default on the date the PFS transaction closes, pursuant to section 204(a)(1)(D) of the National Housing Act, 12 U.S.C. 1710.
- PFS transactions are reported to consumer reporting agencies and will likely affect the Borrower's ability to obtain another Mortgage and other types of credit.
- If the Borrower is a servicemember, it is recommended that the Borrower obtain guidance from their employer regarding the PFS's impact on their security clearance and employment.

Where the Property is encumbered with a PACE obligation, 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 buyer in accordance with applicable law (state and local) and made part of the sales contract.

Pre-Foreclosure Sales – Owner-Occupant Borrower Compensation – Use of Compensation (III.A.2.1.ii.(D)(2))

The Owner-Occupant Borrower may:

- apply the entire amount of the \$3,000 compensation or a portion of it to resolve liens, including a PACE obligation; and/or
- offset the sales transaction costs not paid by HUD (including a home warranty plan fee, costs of optional repairs, and the buyer's closing expenses).

The Mortgagee must instruct the Closing Agent to:

- pay the HUD relocation or transition assistance from Net Sale Proceeds; and
- itemize on the Closing Disclosure or similar legal document any relocation or transition assistance received by HUD or from other entities.

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Pre-Foreclosure Sales – Property List Price and Valuation – Appraisals – Required Analysis and Reporting of a PACE Obligation

(III.A.2.1.ii.(G)(2)(c))

The Appraiser must review the sales contract and property tax records for the Property to determine the amount outstanding and the terms of the PACE obligation:

- if the Mortgagee notifies the Appraiser that the subject Property will remain subject to a PACE obligation,
- when the Appraiser observes that the property taxes for the subject Property are higher than average for the neighborhood and type of dwelling, or
- when the Appraiser observes energy-related building components or equipment or is aware of other PACE-allowed improvements during the inspection process.

The Appraiser must report the outstanding amount of the PACE obligation for the subject Property and provide a brief explanation of the terms.

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 value of the Property, whether positive or negative, of the PACE-related improvements and any additional obligation (i.e., the PACE special assessment).

Deed-in-Lieu of Foreclosure – Eligibility – Condition of Title

(III.A.2.1.iii.(B)(3))

The Borrower or Mortgagee must be able to convey a clear and marketable title to the Secretary. The Mortgagee must obtain a title search or preliminary report and **determine whether** the title is impaired by:

- unresolvable title problems;
- liens that cannot be discharged as permitted by HUD; or
- **a PACE obligation.**

Deed-in-Lieu of Foreclosure – DIL Borrower Consideration – Use of Consideration Amount (III.A.2.1.iii.(E)(2))

The Owner-Occupant Borrower may apply the entire amount of the consideration or a portion of it to resolve **liens, including PACE obligation liens.**

The Owner-Occupant Borrower who is required to make a Cash Reserve contribution may only receive the amount necessary to satisfy **liens**, up to the consideration limit.

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Deed-in-Lieu of Foreclosure – DIL Conveyance to HUD – Discharge of Liens (III.A.2.1.iii.(G)(2))

The Mortgagee must provide for the discharge of liens as follows:

- The Mortgagee must complete a title search and must ensure that the secure release of liens and/or endorsements to the title policy are obtained.
- HUD will not accept titles subject to most liens, including IRS and HOA liens. HUD will allow liens securing repayment of Section 235 assistance payments, Partial Claim advances, and Title I liens.
- HUD will allow a notice of lien recorded in the land records securing repayment of a PACE obligation that may only become subject to an enforceable claim (i.e., a lien) for delinquent regularly scheduled PACE special assessment payments and otherwise complies with the eligibility and acceptability criteria for Properties encumbered with a PACE obligation provided in Section II.A.1.b.iv.(A)(6).
- If the Owner-Occupant Borrower receives consideration, this consideration may be applied towards discharging liens.

Claims Without Conveyance of Title – Property Valuation and CAFMV – Required Analysis and Reporting of a PACE Obligation (III.A.2.p.iii.(A)(3))

The Appraiser must review property tax records for the Property to determine the amount outstanding and the terms of the PACE obligation:

- if the Mortgagee notifies the Appraiser that the subject Property will remain subject to a PACE obligation,
- when the Appraiser observes that the property taxes for the subject Property are higher than average for the neighborhood and type of dwelling, or
- when the Appraiser observes energy-related building components or equipment or is aware of other PACE-allowed improvements during the inspection process.

The Appraiser must report the outstanding amount of the PACE obligation for the subject Property and provide a brief explanation of the terms.

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

Claims Without Conveyance of Title – Property Valuation and CAFMV – Required Documentation (III.A.2.p.iii.(A)(4))

If the Property is to be conveyed to HUD, the Mortgagee must upload into P260 a copy of the appraisal used to determine CAFMV.

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Foreclosure – **PACE Obligation Review (III.A.2.r.i.(H))**

The Mortgagee must:

- review each Property at the time of foreclosure referral to determine if the Property is encumbered with a PACE obligation;
- confirm that any identified PACE obligation may only become subject to an enforceable claim (i.e., a lien) for delinquent regularly scheduled PACE special assessment payments and otherwise complies with the eligibility and acceptability criteria for Properties with a PACE obligation provided in Section II.A.1.b.iv.(A)(6); and
- contact the HUD National Servicing Center for guidance if a noncompliant PACE obligation is identified.

Conveyance of Acquired Properties – Condition of Title – Liens (III.A.2.t.iii.(A))

HUD will not accept title subject to **liens**, other than the following.

(1) **IRS Liens**

HUD will not object to title where there is a lien in favor of the IRS, regardless of its position, if the following conditions are met:

- The IRS has been notified of the foreclosure.
- The IRS lien was established after the date of the mortgage lien.
- The Mortgagee bid at least the full amount of the indebtedness plus the cost of foreclosure.

(2) **Section 235 Liens**

HUD will accept title subject to a junior lien securing the repayment of Section 235 assistance payments.

(3) **PACE Obligation**

HUD will allow a notice of lien recorded in the land records securing repayment of a PACE obligation that may only become subject to an enforceable claim (i.e., a lien) for delinquent regularly scheduled PACE special assessment payments and otherwise complies with the eligibility and acceptability criteria for Properties encumbered with a PACE obligation provided in Section II.A.1.b.iv.(A)(6).

Conveyance of Acquired Properties: Taxes at Conveyance – Standard (III.A.2.t.iii.(B)(1)(a))

Prior to the conveyance of a Property to HUD, the Mortgagee must satisfy all taxes **and special assessments, including: any PACE assessments:**

- that are due and payable prior to or on the date of conveyance; or
- due and payable within 30 Days after the date of conveyance.

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Conveyance of Acquired Properties: Taxes at Conveyance – Required Documentation (III.A.2.t.iii.(B)(1)(b))

The Mortgagee must:

- certify that all available tax and assessment bills due at conveyance and within 30 Days of conveyance are paid as of the date of conveyance;
- document such payment and identify the most recent period for which taxes were paid in Item 32, “Schedule of Tax Information,” of form [HUD-27011](#), Part A; and
- upload to [P260](#) documentation, such as a paid receipt or a copy of the Mortgagee’s tax payment history screen, validating that such payment was made.

The Mortgagee must also retain invoices, paid bill receipts, or other proof of payment in the Claim Review File.

Assumptions – Communication with Borrowers Regarding Assumptions (III.A.3.b.vii.)

Upon any inquiry by a seller regarding HUD’s assumption requirements or upon learning that an assumption has occurred, the Mortgagee must:

- attempt to obtain the forwarding address of the selling Borrower;
- advise the selling Borrower to update the mailing address as needed; and
- advise the selling Borrower that any existing PACE obligation that will remain with the property must be fully disclosed to the buyer in accordance with applicable law (state and local) and made part of the sales contract.

**Information
Collection
Requirements**

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 Numbers 2502-0059, 2502-0306, and 2502-0589. 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

Any questions regarding this Mortgagee Letter may be directed to the HUD National Servicing Center at (877) 622-8525. Persons with hearing or speech impairments may reach this number by calling the Federal Relay Service at (800) 877-8339. For additional information on this Mortgagee Letter, please visit www.hud.gov/answers.

Signature

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