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COMMENT

PICKING UP THE PACE: REVITALIZING A PRIVATE, MARKET-DRIVEN SOLUTION TO RISING ENERGY COSTS AND ENVIRONMENTAL POLICY

Brian R. Giaquinto[†]

ABSTRACT

Since the energy crisis of 1973, Americans have steadily beaten the energy independence drum. The escalating costs of energy, in recent years, provided renewed vigor to the debate regarding energy consumption. Renewable energy, conservation, and efficiency projects come with hefty, upfront costs that hinder the average homeowner's attempt to individually address energy issues. In answer to this problem, and in spite of the fruitless debate among politicians and environmental activists, a new program emerged: Property Assessed Clean Energy ("PACE"). PACE is a local government initiative with unique legal consequences. In keeping with the principles of federalism, states authorize their municipalities to create special tax assessment districts, which allow bonds to be issued. A property owner receives money from the bond issuance to make the qualified improvements. Then, the property owner repays the amount he borrowed through an incremental increase on his property tax bill. The PACE loan creates an appurtenant lien on the property. Since its inception, twenty-six states and the District of Columbia have enacted PACE enabling statutes that serve each jurisdiction's unique needs and energy goals. This rapid support of PACE is bolstered by support from the White House and the Department of Energy.

Two unique challenges, however, hinder PACE. First, the Federal Housing and Finance Agency ("FHFA") stated that it will not allow Fannie Mae or Freddie Mac to finance PACE-encumbered mortgages. The agency feared it would not get paid in the event of foreclosure. Second, states and municipalities rely on public funding despite the original intent that PACE be funded solely by private investment. In the wake of the recent foreclosure crisis in America, this reliance on public funding proved detrimental. Declining property values translated to declining tax revenues. Because of

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this decline, municipalities can no longer afford to issue new PACE bonds. These obstacles caused PACE to grind to a halt.

To overcome these obstacles, states should amend their statutes to allow private developers to fund PACE within their communities. Common-interest communities (“CICs”) are authorized by enabling statutes to make costly infrastructure improvements on behalf of the municipality. The municipalities repay the communities by assessing the property owner an incremental tax increase. Since property assessments are appurtenant, they remain attached to the property. Like the current tax assessment paradigm, owners who enjoy PACE funding can repay the developer through *non ad valorem* property tax assessments.¹ The developer will realize market-driven returns on the investment without having to be a bill collector. Because most mortgages—if not all—in CICs are non-FHFA, there is no conflict with the agency. A corollary to this proposal is for municipalities to utilize incentives to entice private investors who will fund PACE in areas outside of a CIC.

PACE is an outstanding program that promotes energy security and independence with little federal regulation. PACE solves the problem of high upfront costs that hinder the average homeowner. With the suggested modifications and extensions to the current PACE paradigm presented in this Comment, PACE can once again be available and active throughout the United States.

I. INTRODUCTION

The following is an increasingly common news report: “Energy costs for U.S. households will almost double this year from 2001, consuming a fifth of the annual income for half of American homes”² Americans struggle

1. American Jurisprudence describes the phrase *ad valorem*:

The phrase “ad valorem” means, literally, “according to the value,” and is used in taxation to designate an assessment of taxes against property, real or personal, at a certain rate upon its value. An ad valorem property tax is invariably based upon ownership of property, and is payable regardless of whether the property is used or not, although the value may vary in accordance with such a factor.

71 AM. JUR. 2D *State and Local Taxation* § 18 (2012) (citations omitted). Such a tax is neither intended nor expected to be passed on, although under some circumstances, as with rental property, this may be done.

2. Jim Snyder & Mark Drajem, *Energy Takes Twice As Much Income for Half of U.S. Households*, BUSINESSWEEK (Feb. 9, 2012, 12:14 PM),

to control dramatically increasing energy costs. The problem, however, is that energy improvements often come with prohibitively high upfront costs. States are also increasingly reluctant to accept the one-size-fits-all approach of those federal environmental regulations that have little relevance to local environmental problems. Yet, there is a proven solution that can help states and individuals take control of energy costs and environmental policy: Property Assessed Clean Energy (“PACE”). PACE is an innovative financing arrangement where a property owner pays for the upfront costs of energy improvements with money from a loan that is repaid by an incremental increase on his property tax bill. PACE swept across the nation like a wildfire. In three years, twenty-six states and the District of Columbia created unique PACE enabling statutes that serve their individual needs and energy goals.³ The recent subprime mortgage crisis and regulatory suspicion, however, hampered PACE progress. With the right statutory modifications, PACE will return to the forefront of state environmental policy.⁴

This Comment begins by introducing the PACE program and its incredibly rapid adoption across the nation.⁵ Next, this Comment analyzes the legal authority for establishing PACE.⁶ In addition to statutory authority, this Comment addresses the competing ideas of federalism and federalism’s impact on environmental regulation.⁷ Next, this Comment analyzes the problems and controversies that have brought PACE to a grinding halt.⁸ Last, this Comment proposes extending PACE statutes to allow private developers to fund PACE projects within their own developments.⁹ This is a logical extension to PACE because (1) it is consistent with current tax assessment authority, (2) it avoids the FHFA controversy, and (3) it empowers states and individuals to control environmental policy and energy costs.

<http://www.businessweek.com/news/2012-02-09/energy-takes-twice-as-much-income-for-half-of-u-s-households.html>.

3. See *infra* Part II.A.2.

4. See *infra* Part III.

5. See *infra* Part II.A.

6. See *infra* Part II.B.

7. See *infra* Part II.B.2.

8. See *infra* Part II.C.

9. See *infra* Part III.

II. BACKGROUND

A. *Property-Assessed Clean Energy*

1. Program Basics

PACE is a loan program that finances renewable energy or energy efficiency home improvements.¹⁰ Its primary purpose is to ease the significant upfront costs associated with energy improvements.¹¹ An incremental increase on the participating owner's property tax bill repays the loan, often at a very low interest rate.¹² The term for PACE financing is up to twenty years but no longer than the useful life of the improvement.¹³ An appurtenant, first-priority lien¹⁴ guarantees repayment of the total loan cost.¹⁵ If an owner fails to pay off the PACE tax assessment before selling the property, then the new owner assumes the obligation.¹⁶ The first-priority lien ensures that the PACE loan is paid before any non-tax claims in the event of foreclosure.¹⁷

States establish PACE by granting municipalities the authority to create special assessment districts ("SADs"),¹⁸ define qualified improvement projects, and issue bonds to raise capital.¹⁹ SADs typically overlay traditional assessment districts that finance local improvements such as

10. Jason R. Wiener & Christian Alexander, *On-Site Renewable Energy and Public Finance: How and Why Municipal Bond Financing is the Key to Propagating Access to On-Site Renewable Energy and Energy Efficiency*, 26 SANTA CLARA COMPUTER & HIGH TECH. L.J. 559, 574 (2010).

11. Joel B. Eisen, *Can Urban Solar Become a "Disruptive" Technology?: The Case for Solar Utilities*, 24 NOTRE DAME J.L. ETHICS & PUB. POL'Y 53, 84 (2010).

12. *Natural Res. Def. Council, Inc. v. Fed. Hous. Fin. Agency*, 815 F. Supp. 2d 630, 633 (S.D.N.Y. 2011); Wiener & Alexander, *supra* note 10, at 574.

13. *Natural Res. Def. Council, Inc.*, 815 F. Supp. 2d at 633.

14. *See id.* The court also noted that, "Because first lien status is critical to the success of PACE programs, eliminating the priority lien status would make PACE programs effectively impossible to finance through the capital markets." *Id.*

15. Wiener & Alexander, *supra* note 10, at 574-75.

16. Eisen, *supra* note 11, at 85. A more detailed analysis of the economics of land-sales contracts is beyond the scope of this Comment.

17. Wiener & Alexander, *supra* note 10, at 575.

18. SAD is a general term. Some jurisdictions have chosen to give the districts a unique name. *See* Wiener & Alexander, *supra* note 10, at 577 (noting that the city of Berkeley, California, named its district a "Sustainable Energy Financing District").

19. Eisen, *supra* note 11, at 84.

schools, roads, and water-retention facilities.²⁰ After establishing a PACE SAD, the municipality raises the needed funds by issuing tax-exempt bonds,²¹ which are backed by first-priority liens.²² These bonds can be an attractive investment option.²³ Everyone benefits when PACE is allowed to operate: the property owner receives the benefit of lowered energy costs with little or no upfront expense, the investor receives a guaranteed investment return, and the community receives an improved environment.

2. PACE Adoption and Motivation

PACE adoption begins when the state legislature, by statute or otherwise, grants authority to local governments to initiate PACE tax assessments.²⁴ Twenty-six states and the District of Columbia enacted legislation to authorize PACE. Hawaii, however, permits PACE based on a pre-existing statute.²⁵ The following table lists PACE legislation by date of enactment:

PACE Enabling Bills Passed between 2008-2011²⁶

<u>State (Legislation)</u>	<u>Date of Legislation</u>
California (A.B. 811)	2008
Colorado (H.B. 08-1350)	2008
Virginia (S.B. 1212)	2009
Maryland (H.B. 1567)	2009
Oklahoma (S.B. 668)	2009
New Mexico (H.B. 572)	2009
Wisconsin (A.B. 255)	2009

20. Wiener & Alexander, *supra* note 10, at 570.

21. *Id.* at 572.

22. *Id.* at 573.

23. *Id.* at 572–73; *see also supra* notes 14–15 and accompanying text.

24. *See About PACE, PACENow*, <http://pacenow.org/about-pace/> (last visited Oct. 6, 2012); *see also* CAL. PUB. RES. CODE § 26100 (West 2011) (justifying PACE by the public policy benefits of “job creation, lower energy demand, and spurring new clean industries that will grow the economy”); FLA. STAT. ANN. § 163.08 (West 2009) (noting that PACE assessments foster “the public policy of the state to play a leading role in developing and instituting energy management programs that promote energy conservation, energy security, and the reduction of greenhouse gases”); Wiener & Alexander, *supra* note 10, at 575.

25. *PACE Financing Map*, DSIRE: DATABASE OF STATE INCENTIVES FOR RENEWABLES & EFFICIENCY (Aug. 2012), http://www.dsireusa.org/documents/summarymaps/PACE_Financing_Map.pdf.

26. *Id.*; *see also* Ian M. Larson, Law Summary, *Keeping Pace: Federal Mortgage Lenders Halt Local Clean Energy Programs*, 76 MO. L. REV. 599, 604 (2010) (providing a similar but incomplete table of enactments).

Nevada (S.B. 358)	2009
Vermont (H. 161)	2009
Texas (H.B. 1937)	2009
Louisiana (S.B. 224) ²⁷	2009
Ohio (H.B. 1)	2009
Oregon (H.B. 2626)	2009
Illinois (S.B. 583)	2009
North Carolina (S.B. 97)	2009
New York (S66004A)	2009
Maine (L.B. 1717)	2010
Minnesota (H.F. 2695)	2010
Massachusetts (H.B. 4526)	2010
Michigan (H.B. 5640)	2010
Hawaii (H.B. 2643)	2010
New Hampshire (H.B. 1554)	2010
Missouri (H.B. 1692)	2010
Georgia (H.B. 1388)	2010
Florida (H.B. 7179)	2010
District of Columbia (8-1778.02)	2010
Connecticut (S.B. 1243)	2011

As seen in the table, PACE legislation passed very quickly throughout the United States. Its adoption was driven by four overriding ideas: climate change, economic advantage, simplicity of implementation, and creation stewardship.

a. Climate Change

The federal government's unwillingness to adopt international treaties and resolutions that curb greenhouse gases and halt climate change alarms many environmentalists.²⁸ In the face of federal government inaction, a large number of states enacted their own environmental policies.²⁹ Scholars

27. See *infra* Part II.C (discussing the controversies that prompted Louisiana to repeal its PACE statute).

28. See Ann E. Carlson, *Iterative Federalism and Climate Change*, 103 NW. U. L. REV. 1097, 1097 (2009) (mentioning the federal government's repudiation of the Kyoto Protocol); Committee on Climate Change, Sustainable Development, and Ecosystems, *2010 Annual Report*, 2010 ENV'T, ENERGY, & RESOURCES L.: YEAR REV. 30, 30 (reporting that, while the federal government failed to enact climate change legislation, individual states entered into regional cap-and-trade agreements).

29. Carlson, *supra* note 28, at 1098.

and policymakers offer different theories why the states, despite limited economic incentives, enacted environmental legislation.³⁰ Two theories dominate the debate: the states are either trying to garner political advantage with policymakers in Washington or are trying to create a competitive advantage for economic development.³¹

b. Economic Advantage

The latest economic downturn is forcing property owners and users to create innovative ways to reduce energy costs. Property owners are discovering that lowered energy costs more than compensate for the associated capital investment.³² Policymakers and property owners are finding innovative ways to overcome the presumption that economic growth and stability are only achievable by increasing energy consumption.³³ PACE is an example of that type of innovation. PACE is an investment in energy efficiency that gives property owners greater control over increasingly high energy costs.

c. Simplicity of Implementation

PACE is a new application of existing taxing authority.³⁴ Increased population and development naturally lead to an increased need for expensive infrastructure.³⁵ The most common practice is for local governments to establish a SAD over an existing tax assessment district.³⁶ Municipalities are using SADs more frequently because of budget

30. *Id.* at 1099.

31. *Id.*

32. See John C. Dernbach, Robert B. McKinstry, Jr. & Darin Lowder, *Energy Efficiency and Conservation: New Legal Tools and Opportunities*, NAT. RESOURCES & ENV'T, Spring 2011, at 7.

33. See PACENow, *supra* note 24.

34. See Wiener & Alexander, *supra*, note 10, at 571–72, 574; see also FLA. STAT. ANN. 189.402(3)(a) (West 2009) (noting that special assessment districts help to solve “the state’s planning, management, and financing needs for delivery of capital infrastructure, facilities, and services in order to provide for projected growth without overburdening other governments and their taxpayers”).

35. See Janice C. Griffith, *Special Tax Districts to Finance Residential Infrastructure*, 39 URB. LAW. 959, 960 (2007).

36. See, e.g., FLA. STAT. ANN. 190.00–.049 (West 2009); *Williams v. Anne Arundel Cnty.*, 638 A.2d 74, 75 (Md. 1994) (noting “the long-standing practice in [Maryland] of creating special community benefit tax districts in residential subdivisions in order to finance certain local improvements and services”).

constraints and the inability to raise funds for important projects.³⁷ PACE is an energy-improvement variant of this existing practice.³⁸ Energy SADs are simple to set up, provide a secure means of financing, and operate to further the state's public policy goals.³⁹ Because PACE funds come from bond issuances, PACE programs do not drain a local government's general tax fund.⁴⁰

d. Creation Stewardship

Creation Stewardship is a growing inter-faith movement⁴¹ that articulates Biblical reasons for protecting the environment.⁴² The movement believes that caring for the environment ultimately equates to caring for people. Creation Stewardship seeks to eliminate excessive anthropocentrism,⁴³ which antagonists of Christianity believe is the cause of environmental degradation.⁴⁴ To illustrate how influential Creation Stewardship has become, the Southern Baptist Convention, a politically and doctrinally conservative denomination, adopted a global warming resolution.⁴⁵

Christians are called by God to exercise caring stewardship and dominion over the earth and environment (Genesis 1:28; Psalm 8) . . . [W]e continually reaffirm our God-given responsibility to

37. See *supra* note 34 and accompanying text.

38. Eisen, *supra* note 11, at 84.

39. Wiener & Alexander, *supra* note 10, at 575; PACENow, *supra* note 24.

40. Wiener & Alexander, *supra* note 10, at 583. Municipal debt causes its own share of problems. By funding PACE from a separate bond issuance, the municipality does not have to use its general funds, which are earmarked for other important needs.

41. *Christian Statements on the Environment*, GREENFAITH, <http://greenfaith.org/religious-teachings/christian-statements-on-the-environment> (last visited Oct. 6, 2012) (providing links to various Christian denominations' statements on the environment).

42. Douglas J. Moo, *Eschatology and Environmental Ethics*, in *KEEPING GOD'S EARTH: THE GLOBAL ENVIRONMENT IN BIBLICAL PERSPECTIVE* 23, 24 (Noah J. Toly & Daniel I. Bock eds., 2010); see also *id.* at 24 n.7 (listing a brief survey of prominent evangelical scholars who have contributed to creation stewardship ideas).

43. See David Gushee, *Environmental Ethics: Bringing Creation Care Down to Earth*, in *KEEPING GOD'S EARTH*, *supra* note 42, at 245, 249–54. Anthropocentrism is literally defined as human-centered. In the context of environmentalism, however, anthropocentrism refers to an attitude that focuses solely on humans to the detriment and indifference of anything else. *Id.*

44. Moo, *supra* note 42, at 23.

45. *On Global Warming*, S. BAPTIST CONVENTION (June 2007), <http://www.sbc.net/resolutions/amResolution.asp?ID=1171>.

care for the earth by remaining environmentally conscious and taking individual and collective efforts to reduce pollution, decrease waste, and improve the environment in tangible and effective ways.⁴⁶

According to Douglas Moo, many Christians have a negative view of environmentalism because the New Testament tends to portray the world negatively.⁴⁷ Dr. Moo argues, however, that Romans chapter eight “implies that the destiny of the natural world is not destruction but transformation.”⁴⁸ This hope of transformation and the theological concept of resurrection are at the heart of the Creation Stewardship movement.⁴⁹ Another organization involved in creation stewardship, GreenFaith, seeks to provide faith-based groups with cost-effective environmental solutions.⁵⁰ Notably, the Department of Energy (DOE) works with faith-based groups such as GreenFaith to promote energy conservation.⁵¹ The DOE plays a key role in promoting PACE, despite the fact that PACE gets its authority from state governments.⁵²

B. Authority for PACE Legislation

1. State Statutes

Each state has individual goals, preferences, and attitudes toward environmental regulation and economic development. Because a state can uniquely tailor PACE statutes to suit its needs, PACE works best as a state-

46. *Id.*

47. Moo, *supra* note 42, at 25.

48. *Id.* at 31.

49. *Id.* at 35.

50. *Stewardship*, GREENFAITH, <http://greenfaith.org/resource-center/stewardship> (last visited Oct. 6, 2012) (listing “tools to help religious institutions and their members adopt sustainable consumption habits”).

51. *Leveraging Partnerships with Faith-Based Organizations*, U.S. DEP’T OF ENERGY 9, 26 (May 17, 2011), available at http://www.eere.energy.gov/wip/solutioncenter/pdfs/leveraging_partnerships_with_faith-based_organizations.pdf (listing partnerships with Green Faith, Wesley Theological Seminary, Greater Washington Interfaith Power and Light, Interfaith Conference of Metropolitan Washington, New Psalmist Baptist Church, and Baltimore Jewish Environmental Network).

52. *Property-Assessed Clean Energy (PACE) Programs*, U.S. DEP’T OF ENERGY, <http://www.eere.energy.gov/wip/solutioncenter/financialproducts/pace.html> (last visited Oct. 6, 2012); see also *infra* note 111.

only program. Because states do not operate in a vacuum, there is an inevitable tension between the federal government and the states.

2. *Federalism and State Experimentation*

Federalism limits the ability of the national government to usurp the authority of individual state governments. One commentator notes the following:

One of the most innovative features of the Constitution is the idea that the national government has *only those powers given to it in the Constitution*. By contrast, state governments possess inherent power to act for the perceived good of the state's citizenry so long as those actions comply with (1) the state constitution; (2) valid federal statutory law; and (3) the federal Constitution.⁵³

Justice O'Connor states that "the true 'essence' of federalism is that States as *States* have legitimate interests which the National Government is bound to respect even though its laws are supreme."⁵⁴ These statements highlight two different definitions of federalism: true federalism, which recognizes the freedom to implement unique programs, and states'-rights federalism, which recognizes freedom from federally-mandated minimum standards.⁵⁵ These competing ideas of federalism, like a pendulum, swing back and forth throughout the course of American history.⁵⁶ One commentator observes this phenomenon:

These shifts have tended to parallel shifts in the locus of innovation between the federal government and the state governments. When innovators or progressives control the federal government, the federal government will frequently adopt the innovations developed by similarly progressive states, often at their request. Conflicts will then arise with those states that resist the exercise of federal power to establish a federal

53. CALVIN MASSEY, *AMERICAN CONSTITUTIONAL LAW: POWERS AND LIBERTIES* 127 (3d ed. 2009).

54. *Garcia v. San Antonio Metro. Transit Auth.*, 469 U.S. 528, 581 (1985) (O'Connor, J., dissenting).

55. Robert B. McKinstry, Jr. & Thomas D. Peterson, *The Implications of the New "Old" Federalism in Climate-Change Legislation: How to Function in a Global Marketplace When States Take the Lead*, 20 PAC. MCGEORGE GLOBAL BUS. & DEV. L.J. 61, 110 (2007).

56. *Id.* at 66.

floor. When those opposing an activist role for government control the federal government, conflicts will arise with the more progressive states, whose activities bump up against a federal ceiling established to conserve a uniform national market.⁵⁷

Federalism allows states to create an environment that is conducive to economic development and environmental responsibility, absent expressed or implied preemption by the federal government.⁵⁸ Justice Brandeis suggested that states can act as laboratories for experimental ideas.⁵⁹ States that experiment with novel ideas assume risks that the rest of the nation might be unwilling to bear.⁶⁰ Other states may choose to experiment with the idea if it appears successful in the innovating state. Conversely, other states will abandon the idea if it cannot meet their needs. Thus, courageous and innovative states serve as a model for the nation.⁶¹ The concepts of federalism and state experimentation are critical for understanding the authority to implement PACE and for seeing through the fog of controversy.⁶²

Federalism also applies to environmental regulation. Federal environmental laws adopted in the 1970s began as state regulations.⁶³ State laws were the foundation for the Clean Air Act,⁶⁴ the Clean Water Act,⁶⁵ the Surface Mining Control and Reclamation Act,⁶⁶ and the Comprehensive Response, Compensation and Liability Act.⁶⁷ These state programs were so

57. *Id.*

58. For a detailed analysis of federal preemption, see *supra* note 53, at 318–19; see also JAMES T. O'REILLY, *Federal Preemption of State and Local Law: Legislation, Regulation, and Litigation* 14 (2006).

59. *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) (“[A] single courageous state may, if its citizens choose, serve as a laboratory[,] and try novel social and economic experiments without risk to the rest of the country.”).

60. Carlson, *supra* note 28, at 1103.

61. Justice Brandeis’s terminology is very appropriate in the PACE context because of its unique experimental nature. See *Liebmann*, 285 U.S. at 311.

62. See *infra* Part II.C.

63. McKinstry & Peterson, *supra* note 55, at 67.

64. 42 U.S.C. § 7401 (2011) (establishing air quality enhancement and prevention programs).

65. 33 U.S.C. §§ 1251–1387 (2012) (establishing water pollution prevention programs).

66. 30 U.S.C. §§ 1201–1328 (2012) (preventing adverse environmental impacts from surface coal mining operations).

67. 42 U.S.C. §§ 9601–9675 (2012) (imposing penalties for releasing hazardous materials into the environment); see also McKinstry & Peterson, *supra* note 55, at 67 (noting

successful that federal lawmakers created similar national regulatory programs. Nevertheless, scholars and policymakers debated “whether the federal government or the fifty states are superior environmental policymakers.”⁶⁸ Advocates for national regulation argued that states create only minimal environmental regulations to encourage economic development.⁶⁹ It follows that state regulations would fail to achieve any substantial improvement in the quality of the national environment. Advocates for state regulation argued that solutions must be tailored to fit different environmental conditions among the regions of the nation.⁷⁰ This argument advances the idea that national environmental improvement can be achieved by the states, and that nuanced and custom regulations better address real-world problems than a one-size-fits-all approach. Furthermore, states compete for residents by offering different regulatory and tax incentives⁷¹—creating efficient, market-driven environmental regulation.⁷² PACE is an example of individual states tailoring environmental programs to meet each state’s unique policy goals and needs. The following table illustrates the differing state approaches that pioneered PACE.⁷³

<u>Jurisdiction</u>	<u>Financing Source</u>	<u>Interest</u>	<u>Term</u>	<u>Max. Loan Amt.</u>
Berkeley, CA	\$80 million bond purchase	7.75%	20 years	\$37,500
Palm Desert, CA	City general fund	7%	20 years	None
Sonoma, CA	\$45 million in notes from	U.S. Treasury	* Loans < \$5,000: 5–10	None

that many of the environmental laws developed in the 1970s “were often based on state or regional models developed in the ‘laboratories’ of the more progressive states”).

68. Carlson, *supra* note 28, at 1103.

69. *Id.* at 1104.

70. *Id.* at 1106.

71. *Id.* at 1105.

72. *Id.*

73. Wiener & Alexander, *supra* note 10, at 577–80.

	city treasury	rate plus 4%	years * Loans >\$5,000: 10–20 years	
Boulder, CO	\$40 million in bond purchase	Varies	Varies	\$3,000– \$50,000
Babylon, NY	\$2 million from city's solid waste reserve fund	3% based on the matching savings on energy bill	Varies	\$12,000

Although the basic framework is the same, no jurisdiction has tailored the program exactly alike. Babylon, New York, for instance, provides PACE funding directly to contractors rather than to homeowners.⁷⁴ The ability to adapt programs to local conditions is precisely what Justice Brandeis had in mind and is an important reason why PACE spread so rapidly before recent controversies forced it to a standstill.⁷⁵

C. Problems and Controversies

1. The Federal Housing and Finance Agency Blocks PACE-Encumbered Mortgages.

Congress enacted the Housing and Economic Recovery Act of 2008⁷⁶ to curb the rising numbers of home foreclosures, to prevent financial institutions from failing, and to bolster declining state and local revenue.⁷⁷ This Act created the Federal Housing and Finance Agency (“FHFA”).⁷⁸ Congress charged the FHFA with protecting the financial safety of the

74. *Id.* at 580.

75. *See Liebmann*, 285 U.S. at 311.

76. *Cal. ex rel. Harris v. Fed. Hous. Fin. Agency*, C 10-03084 CW, 2011 WL 3794942, at *1 (N.D. Cal. Aug. 26, 2011).

77. 154 Cong. Rec. E1604-04 (daily ed. July 23, 2008) (statement of Rep. Carolyn McCarthy).

78. Housing & Economic Recovery Act of 2008, Pub. L. No. 110-289, 122 Stat. 2654 (2008) (codified as amended at 12 U.S.C. §§ 4511–4526).

Federal National Mortgage Association (“Fannie Mae”),⁷⁹ the Federal Home Loan Mortgage Corporation (“Freddie Mac”),⁸⁰ and the Federal Home Loan Banks.⁸¹ The FHFA acts as a conservator⁸² to restore the institutions to a sound and solvent condition, to allow them to carry out their missions, and to protect their assets and property.⁸³ Fannie Mae and Freddie Mac together own or guarantee the majority of residential mortgages in the United States.⁸⁴ They hold more than \$6 trillion worth of debt and mortgage related assets.⁸⁵ Given the immense amount of money under the umbrella of these institutions, Fannie Mae and Freddie Mac warrant close oversight. On July 6, 2010, FHFA issued a statement that PACE programs “present significant safety and soundness concerns that must be addressed by Fannie Mae, Freddie Mac and the Federal Home Loan Banks.”⁸⁶ FHFA expressed concern that the first-lien status⁸⁷ of PACE loans would create risk management challenges for lenders, servicers, and mortgage-securities investors.⁸⁸ In short, FHFA feared it would not get paid in the event of a foreclosure—a legitimate concern in a subprime mortgage crisis.⁸⁹ On August 31, 2010, Freddie Mac and Fannie Mae jointly issued a bulletin—citing the FHFA statement—noting that they would no longer purchase

79. 12 U.S.C. §§ 1716–1723 (2012).

80. 12 U.S.C. §§ 1451–1459 (2012).

81. 12 U.S.C. §§ 1421–1449 (2012).

82. 12 U.S.C. §§ 4511(b), 4617(a) (2012); *see also* Cal. *ex rel.* Harris v. Fed. Hous. Fin. Agency, C 10-03084 CW, 2011 WL 3794942, at *1 (N.D. Cal. Aug. 26, 2011) (noting that Fannie Mae and Freddie Mac have been under FHFA conservatorship since September 6, 2008).

83. *Town of Babylon v. Fed. Hous. Fin. Agency*, 790 F. Supp. 2d 47, 50 (E.D.N.Y. 2011) (citing 12 U.S.C. § 4617(b)(2)(D) (2012)).

84. *Id.* at 49.

85. *Id.*

86. Press Release, Fed. Hous. Fin. Agency, FHFA Statement on Certain Energy Retrofit Loan Programs (July 6, 2010), *available at* <http://www.fhfa.gov/webfiles/15884/PACESTMT7610.pdf>.

87. *See supra* Part II.A.1.

88. *See* Press Release, *supra* note 86.

89. Significant evidence, however, shows that foreclosures of homes with energy improvements are very low. *See Town of Babylon*, 790 F. Supp. 2d at 51 (“[T]here has never been a single default on a PACE financed repayment obligation.”); Roberta F. Mann, *Federal, State, and Local Tax Policies for Climate Change: Coordination or Cross-Purpose?*, 15 LEWIS & CLARK L. REV. 369, 388 (2011) (noting a recent study reporting that “energy efficient homes had default and delinquency rates 11% lower than for typical homes”).

mortgages encumbered by a PACE lien.⁹⁰ Mortgages purchased prior to the bulletin would be unaltered.⁹¹ Finally, on February 28, 2011, FHFA instructed Fannie Mae and Freddie Mac to refrain from purchasing PACE-encumbered mortgages and to closely watch for similar programs that would create a first-lien obligation.⁹² Nevertheless, as Jonathan B. Wilson observes, PACE programs remain popular:

Despite the position of FHFA . . . other federal agencies and the White House continued publicly to support PACE programs as a tool for job creation and clean energy growth. In response to the recent FHFA statement, additional state and federal officials have come forward to support continuing PACE programs. California, a state with strong PACE support, has taken specific action against the FHFA's statement.⁹³

In addition to White House support for PACE, Representative Nan Hayworth of New York has introduced the "PACE Assessment Protection Act of 2011."⁹⁴ The purpose of this bill is to "prevent Fannie Mae, Freddie Mac, and other Federal residential and commercial mortgage lending regulators from adopting policies that contravene established State and local [PACE] laws."⁹⁵ The bill establishes procedures, financial rules, and credit criteria for an eligible PACE program.⁹⁶ It is likely, however, to remain in committee for the foreseeable future due to the upcoming presidential election.⁹⁷

90. *Town of Babylon*, 790 F. Supp. 2d at 52.

91. *Id.*

92. *Id.* at 52–53.

93. Jonathan B. Wilson et al., *The Great Pace Controversy, Renewable Energy Financing Program Hits A Snag*, PROB. & PROP., May-June 2011, at 38, 40. The Department of Energy has promoted PACE since its initial development. See SOLUTIONS CTR., DEP'T OF ENERGY, <http://www.eere.energy.gov/wip/pace.html> (last visited Mar. 10, 2012) (providing a timeline of the Department's support of PACE). When the FHFA controversy began, the Department strongly voiced its objections to the ruling. *Id.* The Department is now working with lawmakers to create solutions to overcome the FHFA stalemate; however, creating solutions to the current economic crisis has taken precedence. *Id.* The inconsistent positions taken by the FHFA and the Department of Energy have created a cloud of uncertainty for state legislators and private investors.

94. PACE Assessment Protection Act of 2011, H.R. 2599, 112th Cong. (2011).

95. *Id.*

96. *Id.* § 5.

97. The bill has remained in the Subcommittee on Insurance, Housing and Community Opportunity since August 2011. See H.R. 2599: *PACE Assessment Protection Act of 2011*,

2. PACE Litigation

Since the FHFA ruling, several lawsuits challenged the agency's decision.⁹⁸ The courts in each case had to decide whether FHFA acted as a regulator or as a conservator when it issued the statement to Fannie Mae and Freddie Mac.⁹⁹ The distinction is important because federal law precludes judicial review when FHFA acts as a conservator.¹⁰⁰ Two cases—*Natural Resources Defense Council, Inc. v. Federal Housing & Finance Agency*¹⁰¹ and *Town of Babylon v. Federal Housing & Finance Agency*¹⁰²—held that FHFA acted as a conservator.¹⁰³ Conversely, *California ex rel. Harris v. Federal Housing & Finance Agency* stated that FHFA acted with regulatory power when it issued the February 2011 letter.¹⁰⁴ This latter court ordered FHFA to initiate the notice and comment process—something it previously failed to do—but did not order withdrawal of the July 2010 statement or the February 2011 letter.¹⁰⁵

GOVTRACK.US, <http://www.govtrack.us/congress/bill.xpd?bill=h112-2599> (last visited Oct. 20, 2011).

98. See, e.g., *Cal. ex rel. Harris v. Fed. Hous. Fin. Agency*, C 10-03084 CW, 2011 WL 3794942 (N.D. Cal. Aug. 26, 2011); *Natural Res. Def. Council, Inc. v. Fed. Hous. Fin. Agency*, 815 F. Supp. 2d 630 (S.D.N.Y. 2011); *Town of Babylon v. Fed. Hous. Fin. Agency*, 790 F. Supp. 2d 47 (E.D.N.Y. 2011). These are the most notable cases and are representative of other cases involving FHFA and PACE.

99. See *Cal. ex rel. Harris*, 2011 WL 3794942, at *8 (holding that FHFA was not acting as a conservator); *Natural Res. Def. Council, Inc.*, 815 F. Supp. 2d at 642 (holding that FHFA's letter amounted to conservatorship power); *Town of Babylon*, 790 F. Supp. 2d at 54 (“[T]he acts sought to be nullified here were undertaken pursuant to FHFA’s broad and important statutory charge as conservator”).

100. 12 U.S.C. § 4617(f) (2012).

101. *Natural Resources Defense Council, Inc. v. Federal Housing & Finance Agency*, 815 F. Supp. 2d 630 (S.D.N.Y. 2011).

102. *Town of Babylon v. Federal Housing & Finance Agency*, 790 F. Supp. 2d 47 (E.D.N.Y. 2011).

103. See *id.* at 54; *Natural Res. Def. Council, Inc.*, 815 F. Supp. 2d at 642.

104. See *Cal. ex rel. Harris*, 2011 WL 3794942, at *8.

105. *Id.* at *18; see also 5 U.S.C. 553(b)–(c) (2012) (requiring that administrative agencies, as a prerequisite of the rule-making process, give general notice of the proposed rule in the Federal Register and allow interested people to submit information regarding the subject of the ruling); 5 U.S.C. 706(2)(d) (2012) (allowing a reviewing court to set aside an agency action if it has not complied with proper procedure).

3. Public Funding Is Withering Away.

Although the intention of PACE statutes is for private investment to fund PACE bonds,¹⁰⁶ many states relied primarily on public funding. Public funding came from three sources: the American Recovery and Reinvestment Act of 2009 (“ARRA”),¹⁰⁷ state legislatures, and local municipalities.

a. American Recovery and Reinvestment Act of 2009¹⁰⁸

ARRA is designed to create jobs, to promote economic recovery, and to invest in environmental protection that will also provide long-term economic benefits.¹⁰⁹ The federal tax code, prior to ARRA, prohibited anyone from receiving federal energy subsidies.¹¹⁰ ARRA changed the code to allow subsidies for individuals and businesses that finance renewable energy projects with taxable municipal bonds.¹¹¹ Though intended to be bond-driven, PACE now incorporates alternative funding from state, local, and federal sources. Specifically, ARRA provided the Department of Energy (“DOE”) with \$3.2 billion, stipulating that the funds be available for energy efficiency and conservation block grants.¹¹² The DOE substantially funds PACE programs, as part of the American Recovery and Reinvestment Act of 2008.¹¹³ Through these programs, state and local governments finance improvements with debt obligations secured by the retrofitted properties. “As a related benefit, the programs are intended to create jobs.”¹¹⁴

In fact, DOE gave \$452 million of ARRA funds to retrofit existing buildings and \$30 million for residential, energy-efficiency strategies.¹¹⁵ In

106. Larson, *supra* note 25, at 601, 606 (“[Municipal] bonds allow local governments to finance new energy improvements with private funds. . . . PACE programs are particularly attractive to investors because they offer the added assurance of senior lien status.”).

107. American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat 115. This law was originally entitled the American Recovery and Reinvestment Act of 2008.

108. *Id.*

109. *Id.* § 3.

110. Eisen, *supra* note 11, at 85.

111. *Id.*

112. American Recovery and Reinvestment Act of 2009 tit. IV, 123 Stat 115.

113. *See supra* text accompanying note 107.

114. Cal. *ex rel.* Harris v. Fed. Hous. Fin. Agency, C 10-03084 CW, 2011 WL 3794942, at *1 (N.D. Cal. Aug. 26, 2011).

115. Committee on Smart Growth and Green Buildings, *2010 Annual Report*, 2010 ENV'T, ENERGY, & RESOURCES L.: YEAR REV. 117, 119.

California alone, DOE invested \$150 million in PACE projects.¹¹⁶ Maine received \$30 million from DOE “to help support implementation of its PACE programs statewide.”¹¹⁷ DOE, as part of its commitment to PACE, produced comprehensive “Best Practice Guidelines” that included guidance on loan-to-house-value ratios; minimum threshold costs to be eligible for PACE financing; and specific situations where PACE financing should not be allowed.¹¹⁸ These guidelines ensure a return on investment and fulfill the purposes of ARRA—investing in environmental protection and providing long-term economic benefits.¹¹⁹ This funding, however, has been suspended because of the FHFA controversy.¹²⁰ PACE funding from the federal government, while helpful, is not the only alternative source of funds for PACE programs.

b. State Legislatures and Local Municipalities

Local PACE programs rely heavily on public funding from state and local governments. In addition to the \$150 million ARRA grant discussed above, the California state legislature allocated \$50 million to assist local PACE programs.¹²¹ At the local level, Palm Desert and Sonoma Counties in California began their PACE projects using general fund revenue.¹²² Taking a different track, Babylon, New York allocated \$2 million from the city’s solid waste reserve to fund PACE.¹²³ Despite the willingness of state and local governments to commit resources to PACE, the reality is that the primary source of general revenue for local governments is property taxes.

116. Mann, *supra* note 89, at 388.

117. *Local Option—Property Assessed Clean Energy*, ENERGY.GOV, <http://energy.gov/savings/local-option-property-assessed-clean-energy> (last visited Mar. 10, 2012).

118. Larson, *supra* note 25, at 617, 621; *see also id.* at 613 n.91 (“[The] guidelines were developed in concert with [Department of Housing and Urban Development], [National Electrical Code], [Department of the Treasury], [Counsel on Environmental Quality], [Office of Management and Budget] and the White House.”).

119. *See supra* note 107, § 3.

120. Committee on Smart Growth and Green Buildings, *supra* note 115, at 119–20; *see also* Part II.C.1 (discussing FHFA’s opposition to a PACE lien).

121. Committee on Climate Change, Sustainable Development, and Ecosystems, *supra* note 28, at 39.

122. DEP’T OF ENERGY, SOLAR POWERING YOUR COMMUNITY: A GUIDE TO LOCAL GOVERNMENTS 50 (2011), available at http://www4.eere.energy.gov/solar/sunshot/resource_center/sites/default/files/solar-powering-your-community-guide-for-local-governments.pdf; *see also* Wiener & Alexander, *supra* note 10, at 578.

123. Wiener & Alexander, *supra* note 10, at 580.

Unfortunately, the foreclosure crisis negatively impacted PACE implementation.¹²⁴ According to the United States General Accounting Office, foreclosures increased 370 percent from January 2006 to December 2010¹²⁵—1.6 million houses have been lost to foreclosure since 2010.¹²⁶ The Center for Responsible Lending estimates that thirteen million houses will end up in foreclosure by 2015.¹²⁷ Mortgage foreclosures significantly impact PACE. Foreclosed houses that cannot be resold are left vacant, lowering the house's value and the value of houses in the surrounding neighborhood.¹²⁸ The value of those surrounding houses can plummet by as much as ten percent.¹²⁹ Lower values mean lower tax assessments. Lower tax assessments mean lower tax revenues.¹³⁰ As a result, states and municipalities have less money to spend for general on-going projects, let alone PACE projects.¹³¹

124. See BLACK'S LAW DICTIONARY 674 (8th ed. 2004) (defining a foreclosure as “[a] legal proceeding to terminate a mortgagor’s interest in property, instituted by the lender (the mortgagee) either to gain title or to force a sale in order to satisfy the unpaid debt secured by the property”). Certainly, there are other problems inherent with state and municipal funding of PACE programs. The section focuses mainly on the effect that foreclosures have on general tax revenues.

125. GOV'T ACCOUNTABILITY OFFICE, MORTGAGE FORECLOSURES: DOCUMENTATION PROBLEMS REVEAL NEED FOR ONGOING REGULATORY OVERSIGHT 1 (2011), available at <http://www.gao.gov/assets/130/126215.pdf>.

126. Peter King, *1 In 5 Predicted to Default*, NASDAQ (Sept. 20, 2011, 7:03 PM), <http://community.nasdaq.com/News/2011-09/1-in-5-predicted-to-default.aspx?storyid=95228>.

127. Courtney Hunter, *Reducing the Spillover Costs of Foreclosure: Boston's Block-By-Block Approach to Saving Neighborhoods from Foreclosure Blight*, 29 REV. BANKING & FIN. L. 533, 538 (2010).

128. *Id.* at 534; see also Oren Bar-Gill, *The Law, Economics and Psychology of Subprime Mortgage Contracts*, 94 CORNELL L. REV. 1073, 1136 (2009) (“[W]hen foreclosures are clustered, they can injure entire communities by reducing property values in surrounding areas.”).

129. Hunter, *supra* note 127, at 534.

130. *Id.*; see also 72 AM. JUR. 2D *State and Local Taxation* § 642 (2011) (“The ultimate purpose of property valuation is to arrive at a fair and realistic value of property being taxed. . . . Property must be assessed at its just value, and owners of property must bear an equal proportion of the tax burden in proportion to the amount of property owned.” (footnotes omitted)); *Id.* § 628 (“The process for fixing the value of property for tax purposes involves three steps and is exclusive: (1) taxable property is put on the tax roll, (2) value is determined, and (3) a review of such determination is through the tax board and the court system.”).

131. See Hunter, *supra* note 127, at 534. A discussion of foreclosure’s secondary effects, such as rising crime and neighborhood blight, is beyond the scope of this Comment.

As mentioned before, enabling statutes authorize municipalities to raise needed money by issuing tax-exempt bonds.¹³² Although a municipality can raise the desperately needed money through bond issuances, this funding will inevitably be used to support its general obligations, from roads to schools to emergency services.¹³³ Even if the municipality could sell enough bonds to meet all its obligations, the interest on the bonds—including PACE bonds—is paid from tax revenue.¹³⁴ Furthermore, “[i]ncreasing a community’s total debt obligation . . . can result in a lower credit rating for the community.”¹³⁵ Arlington County, Virginia serves as an example of this problem:

Virginia was one of the many states to authorize PACE. But Arlington County, perhaps the most progressive community in the state, is on record as having no plans to create a local [PACE] program because of debt concerns. “Arlington is unlikely to float its own bonds for this, as the County is facing its self-imposed debt ceiling to maintain the coveted Triple-A bond rating.”¹³⁶

Because of the enormous economic challenges that state and local governments face, reliance on public funding of PACE—federal and local—needs to change. Representative Steve Israel of New York submitted a bill designed “[t]o authorize the Secretary of Energy to provide credit support to enhance the availability of private financing for clean energy technology deployment.”¹³⁷ Nevertheless, this bill has remained in committee since 2009.¹³⁸ Despite the difficulties it faces, PACE is an outstanding program that promotes energy efficiency with little federal regulation.¹³⁹ With the right modifications and extensions to the current PACE paradigm, PACE can once again be available and active throughout the United States.

132. See Part II.A.

133. Wilson et al., *supra* note 93, at 39.

134. Larson, *supra* note 26, at 601–02.

135. Wilson et al., *supra* note 93, at 39.

136. *Id.*

137. H.R. 3836, 111th Cong. (2009).

138. This bill has remained in the House Subcommittee on Energy and Environment. H.R. 3836, GOVTRACK.US, <http://www.govtrack.us/congress/bill.xpd?bill=h111-3836> (last visited Mar. 8, 2012).

139. Wilson et al., *supra* note 93, at 39.

III. PROPOSAL

The FHFA controversy and the misguided reliance on public funding forced PACE to a grinding halt in spite of its success across the country. Without programs like PACE, states face hindrances in accomplishing their energy and environmental goals. This void will inevitably be filled by overly burdensome national regulations that apply a one-size-fits-all approach that has little relevance to unique state issues.¹⁴⁰ Property owners are likely to forego improvements that will reduce their energy bills because they will have to bear the brunt of high upfront costs.¹⁴¹ PACE, however, can be reinvigorated with Private Developer PACE. This solution envisions extending all PACE enabling statutes to allow private developers to fund PACE projects within their own developments.

A. *Private Developer PACE Is Consistent with Current Tax Assessment Authority.*

As established above, local governments have the authority to create SADs to fund infrastructure improvements.¹⁴² “As of 2002, more than 35,000 [SADs] had been incorporated . . . [compared to] the country’s 88,525 local governments.”¹⁴³ SADs are particularly attractive because local governments do not have to raise taxes to pay for infrastructure improvements in new residential areas.¹⁴⁴ Privatization is the essence of the traditional SAD because the residents who directly benefit from the improvement—not the local government—pay the infrastructure costs.¹⁴⁵ One key feature of the SAD is the authority to raise money as it sees fit.

[SADs] have been empowered just like general units of local government to levy taxes, assessments, and user charges to effectuate the financing and maintenance of public improvements.

....

140. McKinstry & Peterson, *supra* note 55, at 87 (noting that states have “the ability to develop more narrowly drawn targets that are appropriate for the region”).

141. Eisen, *supra* note 11, at 83.

142. *See supra* Part II.A.1.

143. Griffith, *supra* note 35, at 982 n.1.

144. *Id.* at 962. Enabling statutes empower SADs to finance projects such as roads, sewer systems, water systems, street lights, schools, and fire stations. *Id.* at 967–68.

145. *Id.* at 966.

Special assessments may be levied to provide a revenue stream . . . to maintain the facilities and projects of a district.¹⁴⁶

Privatization of infrastructure improvements is most often found in the common interest community (“CIC”). “The [CIC] is a type of private housing project organized within an association created by either statute or covenants running with the land, whose membership consists of holders of units in the development.”¹⁴⁷ The SAD, through an elected board, manages infrastructure projects for the development.¹⁴⁸ If a large CIC is developed slowly, the developer may serve as the SAD chairperson.¹⁴⁹ Improvement costs are repaid through special assessments on the property owner’s tax bill.¹⁵⁰ Some improvements require a one-time assessment, while others are ongoing and remain the property owner’s obligation.¹⁵¹

PACE programs are strikingly similar to the CIC SAD paradigm.¹⁵² PACE statutes can be easily modified to allow developers, or investors in partnership with the developer, to finance PACE projects within their own CICs. Once the SAD is established, the developer can pool the money under the SAD’s control and designate it for PACE financing. The developer, as the investor and SAD chairperson, would establish the PACE terms. These terms may include loan-to-value ratios, repayment length, credit history requirements, and interest rates. Because PACE is a voluntary, opt-in program, the free market will play a key role in defining the terms. Participation in the program helps the developer determine rates of return. If the rate is set too high, fewer homeowners will participate. Equilibrium is established when the developer discovers the greatest level of participation at a rate he is willing to accept. Financing recipients can then make energy improvements to their homes, such as new appliances or solar panels. The

146. *Id.* at 969.

147. Mark Fenster, *Community by Covenant, Process, and Design: Cohousing and the Contemporary Common Interest Community*, 15 J. LAND USE & ENVTL. L. 3, 4 (1999). The author’s use of the term “association” is synonymous with SAD.

148. Griffith, *supra* note 35, at 972.

149. On Top of the World Communities and The Villages—two large 55-plus CICs in Florida—are representative examples. See *Board of Supervisors*, BAY LAUREL CTR. CDD, <http://www.blccdd.com/the-board.html> (last visited Mar. 10, 2012) (listing developer Kenneth D. Colen as the chairman) (CDD is synonymous with SAD); *About Us*, THE VILLAGES, <http://thevillages.com/AboutUs/aboutus.htm> (last visited Feb. 8, 2012) (noting that the developer remained an integral part of the community).

150. See Wiener & Alexander, *supra* note 10, at 572.

151. Griffith, *supra* note 35, at 977.

152. See *supra* Part II.A.

property owner will repay the developer through a special assessment on the tax bill.¹⁵³ The local government will give the SAD the portion of the tax payment attributable to the PACE financing.¹⁵⁴ The SAD then repays the developer. The property owner gets the benefit of reduced energy costs and the developer gets an acceptable, guaranteed return on investment without being a bill collector.¹⁵⁵ The developer also receives a competitive advantage over other communities that do not offer PACE financing. Profit incentive motivates developers to create CICs that offer the amenities people desire. In sum, Private Development PACE is an attractive amenity because it helps keep energy costs under control while contributing to environmental responsibility. Moreover, the recent PACE obstacles do not affect Private Development PACE.¹⁵⁶

B. Private Development PACE Avoids the FHFA Controversy.

As established above, FHFA instructed Fannie Mae and Freddie Mac to refuse PACE encumbered mortgages.¹⁵⁷ Fannie Mae and Freddie Mac operate in the secondary mortgage market.¹⁵⁸ The primary mortgage market is where the mortgage originates and where the homeowner receives the money to buy a home.¹⁵⁹ The secondary market is where investors purchase mortgages¹⁶⁰—Fannie Mae and Freddie Mac operate in this secondary market. Fannie Mae's and Freddie Mac's primary purpose is to create liquidity in the mortgage market.¹⁶¹ They purchase mortgages from the primary market so that lenders will have the necessary capital to create new

153. Wiener & Alexander, *supra* note 10, at 574.

154. For example, Florida statutes provide that SAD assessments will be “collected in the same manner and same time as county taxes.” FLA. STAT § 190.021(1) (2009). Moreover, the county tax collector is ultimately responsible for collecting the taxes. FLA. STAT. § 197.3632(8)(b)–(c) (2012).

155. The apportionment of the lien guarantees that the developer will be repaid. *See supra* Part II.A.1.

156. *See infra* Part III.B.

157. *See supra* Part II.C.1.

158. *Natural Res. Def. Council, Inc. v. Fed. Hous. Fin. Agency*, 815 F. Supp. 2d 630, 634 (S.D.N.Y. 2011).

159. Bradley K. Krehely, *Government Sponsored Enterprises: A Discussion of the Federal Subsidy of Fannie Mae and Freddie Mac*, 6 N.C. BANKING INST. 519, 523 (2002).

160. *Id.*

161. *Id.*

mortgages.¹⁶² Nevertheless, Fannie Mae and Freddie Mac also conducted lending in the subprime mortgage market.¹⁶³ “The subprime mortgage market involves lending to riskier applicants who have been late on paying monthly credit cards or other debt.”¹⁶⁴ Because of the recent subprime mortgage crisis, FHFA was created to act as conservator to the organizations.¹⁶⁵ As it pertains to PACE-encumbered mortgages, FHFA’s concern is that the institutions will not be repaid in the event of a foreclosure.¹⁶⁶ Because of its senior lien status,¹⁶⁷ PACE loans would be satisfied first.¹⁶⁸ This is precisely why PACE is attractive to investors. Investors are willing to receive below-market rates because PACE essentially guarantees a return.¹⁶⁹

Homeowners in 55-plus communities (“55-plus CICs”) typically have small mortgages, if any at all.¹⁷⁰ “One of the traditional reasons builders have been attracted to [55-plus CICs] is that many of the buyers in this market segment are able to finance their purchases out of accumulated wealth, rather than out of current income.”¹⁷¹ Moreover, 55-plus CICs are steadily growing despite the recent housing decline. According to the National Association of Homebuilders, new housing starts in 55-plus CICs are projected to increase in 2012.¹⁷² Thus, 55-plus CICs are the best place to begin the Private Development PACE solution. Because the vast majority of

162. *See id.*

163. *Id.* at 525.

164. *Id.* at 525 n.51 (citation omitted) (internal quotation marks omitted).

165. *See supra* Part II.C.2.

166. *See supra* Part II.C.1.

167. *See supra* Part II.A.1.

168. *See* *Natural Res. Def. Council, Inc. v. Fed. Hous. Fin. Agency*, 815 F. Supp. 2d 630, 634 (S.D.N.Y. 2011).

169. *See* Wiener & Alexander, *supra* note 10, at 574–75; *see also* *Natural Res. Def. Council, Inc.*, 815 F. Supp. 2d at 633.

170. A recent study indicates that less than 43% of homebuyers in 55-plus CICs require a mortgage. NAT’L ASS’N OF HOMEBUILDERS & METLIFE MATURE MKT. INST., HOUSING TRENDS UPDATE FOR THE 55+ MARKET 63 (2011) [hereinafter NAHB REPORT], available at http://www.nahb.org/fileUpload_details.aspx?contentTypeID=3&contentID=150582&subContentID=315816.

171. *Id.*; *see also* Griffith *supra* note 35, at 972–73 (noting that CICs, which would also include 55-plus CICs, “most likely will attract residents wealthier than the community’s other members because they self select to bear heavier taxation to provide their own facilities”).

172. NAHB REPORT, *supra* note 170, at 6.

55-plus CICs will not have residents who hold a FHFA mortgage, private developer PACE side-steps the FHFA controversy; Private Development PACE reinvigorates PACE and provides needed time for Congress to enact a solution.¹⁷³ Private Development PACE may be an interim solution, but it is a crucial step in working to preserve PACE.

Private Developer PACE would be implemented in CICs that consist of property owners with FHFA mortgages. Individuals who are interested in PACE financing under Private Development PACE would go through an application process.¹⁷⁴ Unfortunately, property owners with FHFA mortgages will not qualify. The developer must inform those homeowners who fail to qualify that their disqualification is due to the FHFA ruling and not a result of a choice made by the developer.

Another facet of Private Development PACE is the need to encourage private investment beyond the gated community. PACE financing is difficult, but not impossible, for property owners outside of the gated community to obtain as long as local governments are willing to implement the appropriate SAD notwithstanding the FHFA ruling.¹⁷⁵ Local governments must seek out private investors rather than rely on public funding for PACE to function in this way.¹⁷⁶ Under Private Development PACE, local governments would be wise to allow investors more control over establishing the terms of the program. Because Fannie Mae and Freddie Mac refuse to purchase mortgages with a PACE encumbrance, homeowners with a government-backed mortgage will not be eligible.

Disqualified property owners who understand the source of the problem and desire a PACE loan can influence Congress to act on the issue. The first step is education. Education will naturally begin during the application process. Program administrators and private developers must inform disqualified homeowners that their disqualification is due to FHFA foreclosure fears. Disqualified homeowners must also be told that energy efficient homes have default and delinquency rates eleven percent lower

173. See generally PACE Assessment Protection Act of 2011, H.R. 2599, 112th Cong. (2011) (providing legislation that will “prevent Fannie Mae, Freddie Mac, and other Federal residential and commercial mortgage lending regulators from adopting policies that contravene established State and local property assessed clean energy laws”). This bill is likely to remain in committee until after the upcoming election cycle.

174. See *supra* Part III.A (noting that private developers, as investors, should establish PACE terms, such as loan-to-value ratios, repayment length, credit history, and interest rates).

175. See *supra* Parts II.A, III.A.

176. See *supra* Part II.C.3.

than typical homes and, in some cities, delinquency never occurs at all.¹⁷⁷ Armed with this information, these homeowners can urge their representatives in Congress to enact legislation that will keep FHFA from blocking PACE loans.¹⁷⁸

C. *Private Developer PACE Empowers States and Property Owners to Control Environmental Policy and Energy Costs.*

States have created some of the most innovative environmental regulations.¹⁷⁹ As discussed above, environmental issues vary by region and cannot be solved by a one-size-fits-all approach.¹⁸⁰ First, states provide a better forum for small businesses to voice their needs and capabilities.¹⁸¹ Second, states can develop programs that are targeted specifically for that region.¹⁸² Third, states are more flexible than the federal government and, therefore, “better able to change strategies if a selected strategy is ineffective or more costly than anticipated.”¹⁸³ If states do not take the initiative to enact environmental legislation, the federal government will fill the regulatory void.

To illustrate, Senator Jeff Bingaman, Chairman of the Senate Committee on Energy and Natural Resources, recently introduced broad-sweeping, national, environmental legislation.¹⁸⁴ The Clean Energy Standard Act of 2012 is designed “to create a market-oriented standard for electric energy generation that stimulates clean energy innovation and promotes a diverse set of low- and zero-carbon generation solutions.”¹⁸⁵ The Act requires large utilities to produce a percentage of the energy they sell from clean energy generators.¹⁸⁶ These clean energy generators are assigned credits corresponding to the level of clean energy output.¹⁸⁷ Even though the Act

177. *See supra* note 89.

178. The PACE Assessment Protection Act of 2011 is an example of such legislation. *See supra* note 94.

179. McKinstry & Peterson, *supra* note 55, at 72.

180. *See supra* Part II.B.2 (noting that most federal environmental programs enacted in the 1970s began as state programs designed to address local conditions).

181. McKinstry & Peterson, *supra* note 55, at 87.

182. *Id.*

183. *Id.* at 88.

184. *See* Clean Energy Standard Act of 2012, S. 2146, 112th Cong. (2012).

185. *Id.* § 610(a).

186. *Id.* § 610(c).

187. *Id.* § 610(f).

does not preempt state clean energy programs,¹⁸⁸ the inevitable consequence will be higher energy costs because utilities will need to purchase new equipment. These new acquisition costs will be passed on to the consumer. This is the opposite of what Americans desperately need and what Private Development PACE can deliver.

PACE is important because it can provide tangible, immediate benefits to the states.¹⁸⁹ Private Developer PACE takes PACE off the regulatory backburner and places it at the forefront of state environmental policy. Private Developer PACE allows individuals to control their energy costs while contributing to environmental responsibility in cost-effective ways.

IV. CONCLUSION

The stakes are high in America. Rising energy costs are eroding the American standard of living. States are increasingly reluctant to accept the one-size-fits-all approach of federal environmental regulations that is barely relevant for local environmental problems. Fortunately, however, PACE is a program that effectively addresses both of these issues. Rapid adoption of PACE programs and the outcry against regulatory suspicion demonstrate the success of this innovative energy program. PACE desperately needs to be reinvigorated. PACE statutes must be modified to allow private developers to fund PACE within their own developments. This proposal is consistent with current tax assessment authority, it avoids confrontation with the FHFA, it catalyzes regulatory change, and, best of all, it allocates control over environmental and energy policy to the proper actors—the states and the people.

188. *Id.* § 610(l).

189. Florida's PACE enabling statute declares that PACE is a vital part of the state's energy conservation policy. FLA. STAT. § 163.08(1)(a) (2010) ("[It is] the public policy of the state to play a leading role in developing and instituting energy management programs that promote energy conservation, energy security, and the reduction of greenhouse gases.").