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IN THE SUPREME COURT OF FLORIDA

FLORIDA BANKERS ASSOCIATION,

Petitioner,

vs.

STATE OF FLORIDA, et al.,

Respondent.

Case No. SC14-1603

L.T. Case No. 14-CA-548

ON APPEAL FROM THE CIRCUIT COURT OF THE SECOND JUDICIAL CIRCUIT IN AND FOR LEON COUNTY, FLORIDA

INITIAL BRIEF OF APPELLANT

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INTRODUCTION

Florida's PACE Act allows property owners to apply for loans from local governments to be used for certain energy related and hurricane mitigation improvements and repairs. When a property owner pays back the loan, he or she does so by paying what the Act characterizes as a "voluntary non-ad valorem special assessment." To have the money to fund these PACE loans, the government sells revenue bonds. Those bonds are then secured by the so-called special assessments the individual property owners have agreed to pay. These "special assessments" are then given priority over other liens on the property, even prior purchase money mortgage liens.

The Appellant, the Florida Bankers Association, challenges the validation of the bonds here because granting superpriority lien rights for the repayment of these loans violates the constitutional rights of prior lienholders. It is impermissible to give later lenders superpriority over earlier lenders that have extended credit under the assumption that they would have the first lien position.

Recognizing this problem, in the PACE Act, the Florida Legislature attempted to describe the loan repayments as "special assessments" rather than loan repayments. This is because, under Florida law, non-ad valorem special assessments are often granted lien priority, even over the liens of earlier-recorded, purchase money mortgagees. While that superpriority infringes upon mortgagees'

constitutional rights, such infringement has been deemed acceptable when a state is exercising its taxing authority by imposing ad valorem taxes or non-ad valorem special assessments.

The Florida Bankers Association demonstrates in this brief that the PACE Act loan repayments are not truly special assessments; they are mere loans. As a result, the rationale that might ordinarily allow some infringement on the constitutional interests of mortgagees no longer applies, and such infringement is prohibited. Thus, the Florida Bankers Association has appealed the trial court's validation of the bonds to be issued pursuant to Florida's PACE Act because the financing arrangement described above that is in place to secure the bonds is prohibited. Such an improper financing arrangement means that there is no authority for the issuance of the bonds, and the bonds cannot be validated.

STATEMENT OF THE CASE AND FACTS

Property Assessed Clean Energy programs, or "PACE" programs, are gaining popularity as a way for local governments to incentivize property owners to invest in property improvements that aid in energy efficiency and conservation. *See* FL Staff An., H.B. 7179, 4/14/2010, Summary Analysis. As part of Florida's stated emphasis on promoting renewable energy, energy conservation, and enhanced energy efficiency, in 2010, Florida passed its own PACE Act. *See* § 163.08(1)(a), Fla. Stat. (2014). Florida's PACE Act also incorporates the state's additional goal of hurricane mitigation. *See* § 163.08(1)(b), Fla. Stat.

Essentially, the PACE Act provides a local government-based financing scheme to propel Florida property owners to invest in "qualifying improvements" to their property. *See generally* § 163.08, Fla. Stat. "Qualifying improvements" include energy-related improvements and wind resistance improvements, such as installation of energy-efficient ventilation systems, electric vehicle charging equipment, solar energy systems, wind-resistant shingles, and other similar types of improvements. § 163.08(2)(b), Fla. Stat. Local governments can incur debt and partner with other local governments to provide the financing to property owners for these qualifying improvements. § 163.08(5)&(7), Fla. Stat. If the local government desires, a qualifying improvement program may be administered by a for-profit entity or a not-for-profit organization. § 163.08(6), Fla. Stat.

To that end, in Florida, we have the Plaintiff/Appellee Florida Development Finance Corporation ("FDFC"), which is a special development finance authority created to cooperate with state public agencies and local governments through interlocal agreements. (A. 3);[1] *see* § 288.9602(8), Fla. Stat. (2014). The FDFC has the authority to enter into, and plans on entering into, such interlocal agreements to finance qualifying improvement projects under the PACE Act. § 288.9606(1)&(7)(c), Fla. Stat. (2014); (A. 4, 20). In keeping with that authority, the FDFC has resolved to finance qualified improvements by creating the Florida Home Energy Renovation Opportunity ("HERO") Program. (A. 3, 22).

The financing process for the FDFC to lend funds to the property owner-borrower under the HERO Program looks like most any other loan. § 163.08(4)-(5) & (8)-(9), Fla. Stat. The process begins when the property owner applies for the loan. § 163.08(4), Fla. Stat. Following the property owner's application, the local government (or Renovate America, Inc., the private entity that will be administering the HERO Program) will essentially do a credit check on the property. § 163.08(9), Fla. Stat.; (A. 20). The property owner has to be current on his or her property taxes and assessments as well as his or her mortgage payments, cannot have involuntary liens on the property, and cannot have recorded property-based debt delinquency. § 163.08(9), Fla. Stat. If these criteria are met, the FDFC

[1] The appendix has been continuously paginated. References are to "A" and the page number.

will enter into a financing agreement with the property owner-borrower. § 163.08(8)-(9), Fla. Stat. The financing agreement is then recorded. § 163.08(8), Fla. Stat.

Interestingly, though, PACE loans give no consideration to the existing loan-to-ratio value. § 168.08(12)(a), Fla. Stat. A property owner may borrow up to 20% of the just valuation of his or her property without any statutory regard for whether the property owner has equivalent equity in the property. § 163.08(12)(a), Fla. Stat. Essentially, then, if the property is already encumbered by a purchase money mortgage for, say, 90% of the appraised value of the property, that means that, after a PACE loan, a property could be encumbered for 110% of its value. § 163.08(12)(a), Fla. Stat. Furthermore, the purchase money mortgagee cannot protect against this diminution in its collateral value by accelerating its loan because the PACE Act prohibits such acceleration if the acceleration is done solely as a result of the property owner obtaining a PACE loan. § 163.08(13), Fla. Stat.

Under the PACE Act, the financing agreement between the property owner and the FDFC provides that the property owner will repay the loan by agreeing to incur what the Florida Legislature has deemed a voluntary non-ad valorem special assessment. *See* §§ 163.08(1)(c); 163.08(4); 163.08(12)-(13), Fla. Stat.; (A. 5). This non-ad valorem special assessment against the property becomes a lien of equal dignity to county taxes and other assessments. § 163.08(8), Fla. Stat.; (A. 6).

Thus, the lien for the repayment of the borrowed funds takes priority over other recorded liens, including preexisting mortgages. § 163.08(8), Fla. Stat.; (A. 9).

To fund these PACE loans, the FDFC resolved to issue revenue bonds. (A. 18-19). The bonds are issued in an aggregate principal amount of up to $2 billion. (A. 2, 18). The FDFC sells the bonds to Renovate America, Inc., the company that that is also acting as the administrator of the HERO program. (A. 20, 238). The money resulting from those bond purchases provides the pool of money that will be available to PACE loan borrowers. (A. 20-21). The repayment of the bonds is secured by the non-ad valorem special assessments agreed to by the property owners when they borrow the money to make the qualified improvements. (A. 4-5).

This appeal arises out of the FDFC's successful complaint for validation of these bonds. (A. 1, 166). In its judgment validating the bonds, the trial court addressed a number of concerns, including the issue of whether the PACE Act's lien superpriority provision unconstitutionally impairs existing mortgage contracts or deprives individuals of protected property interests without due process. (A. 163). The trial court ultimately determined no impermissible constitutional infringement exists, and it validated a number of items, including the bonds, the FDFC Act, the Florida PACE Act, the priority of liens, and the validity of the financing agreements and special assessments. (A. 163, 166).

The Florida Bankers Association has appealed the trial court's amended final judgment, challenging the FDFC's authority to issue the bonds because the PACE Act's financing scheme for securing the bonds is unconstitutional. (A. 169). The Florida Bankers Association is an organization composed of more than 300 banks and financial institutions ranging in size from small community banks and thrifts, to medium sized banks operating in several parts of the state, to large regional financial institutions that are headquartered in Florida or outside the state. As this brief will show, the Florida Bankers Association's members' constitutional interests are in jeopardy due to the PACE Act's method of loan repayment, which, due to its unconstitutionality, renders the FDFC without authority to issue the bonds.

SUMMARY OF THE ARGUMENT

The trial court erred when it validated the bonds to be issued by the FDFC pursuant to Florida's PACE Act. The FDFC is not authorized to issue the bonds because the financing agreement upon which the bonds are secured is unconstitutional. As a result, this Court should reverse.

Florida's PACE Act allows a local government to loan money to an individual property owner to perform energy-related and hurricane mitigation improvements to a property. After the property owner applies for and receives the funds, the property owner and the government enter into a financing agreement that is recorded. Under the terms of the financing agreement, the property owner repays the loan by volunteering to incur a non-ad valorem special assessment. This so-called non-ad valorem special assessment is given lien priority rights over any earlier-recorded, purchase money mortgage.

Because purchase money mortgages are constitutionally protected interests, as a general matter, allowing such lien priority for a later-recorded lien violates the United States and Florida Constitutions. However, the Florida Legislature has attempted to get around that constitutional problem by dubbing the PACE loan repayment a "special assessment." Payment of non-ad valorem special assessments is one of the few exceptions to the prohibition on lien superiority rights against a first-recorded purchase money mortgage.

As this brief shows, a property owner's repayment of a PACE loan is not the payment of a non-ad valorem special assessment. These payments have none of the hallmarks of a special assessment. That is because they are not special assessments; they are mere loan repayments. And, it is settled under Florida law that a mere loan repayment—even one between the government and a property owner given in the name of furthering a legislative policy goal—cannot be a "special assessment" that would be allowed superpriority lien rights.

Thus, because the PACE loan repayments are not actually non-ad valorem special assessments, it is unconstitutional for the liens stemming from those loans to pass over the lien position of an already-recorded mortgagee. Furthermore, because these "special assessments" that are the financial backbone securing the bonds at issue are unconstitutional, the FDFC does not have the authority to issue the bonds. The bonds should not be validated.

STANDARD OF REVIEW

This Court's scope of review in a bond validation case is limited to (i) whether the public body has the authority to issue the bonds in dispute, (ii) whether the purpose of the obligation is legal, and (iii) whether the authorization of the obligation complies with the requirements of law. *City of Gainesville v. State*, 863 So. 2d 138, 143 (Fla. 2003) (citing *State v. City of Port Orange*, 650 So. 2d 1, 2 (Fla. 1994)).

Part of this Court's inquiry into this first issue as to whether a public body is authorized to issue bonds "is the legality of the financing agreement upon which the bond is secured." *Id.* Here, the FDFC pledged non-ad valorem special assessments to secure its revenue bonds. Thus, the FBA's challenge to the validity of these special assessments is properly before this Court. *See id.* ("In this case, the stormwater fees are pledged to repay the bonds. The validity of those fees is the only issue."); *see also State v. Manatee County Port Authority,* 171 So. 2d 169, 171 (Fla. 1965) ("The function of a [bond] validation proceeding is merely to settle the basic validity of the securities and the power of the issuing agency to act in the premises. Its objective is to put in repose any question of law or fact affecting the validity of the bonds.").

In a bond validation appeal, this Court reviews "the trial court's findings of fact for substantial competent evidence and its conclusions of law de novo." *City of Gainesville*, 863 So. 2d at 143.

ARGUMENT

I. THE TRIAL COURT ERRED WHEN IT VALIDATED THE PROPOSED FDFC REVENUE BONDS FOR PACE LOANS BECAUSE THE FDFC DOES NOT HAVE THE AUTHORITY TO ISSUE THE BONDS AS THE FINANCING ARRANGEMENT UPON WHICH THE BONDS ARE SECURED IS UNCONSTITUTIONAL.

The trial court erred when it validated the bonds the FDFC plans to issue pursuant to the PACE Act. The bonds are secured by an unconstitutional financing arrangement, which means that the FDFC does not have the authority to issue the bonds, and validation was improper. The financing arrangement is unconstitutional because it violates the protected rights of purchase money mortgagees by allowing superpriority rights to PACE loan liens. The Act's use of the phrase "non-ad valorem special assessment" to describe how a property owner will repay a PACE loan is not enough to render the Act constitutional.

In this brief, we will show that mortgages are constitutionally protected property interests. We will then demonstrate that, as a result of that protected interest, it is unconstitutional for a legislature to grant superpriority lien rights to a later-recorded lien against an earlier-recorded mortgage lien. While there is an exception to this principle, the exception exists only when the government is exercising its taxing authority, which is not the case here. Finally, we will show how PACE loans are creating real world problems right now, problems that are

illustrative of the rationale underlying the constitutional principles we will discuss below.

Mortgages Are Constitutionally Protected Interests

In Florida, a mortgagee's lien is a constitutionally protected property interest. *See City of Panama City v. Head*, 797 So. 2d 1265, 1267 (Fla. 1st DCA 2001); *Sarasota County v. Andrews*, 573 So. 2d 113, 115 (Fla. 2d DCA 1991); *Mailman Dev. Corp. v. Segall*, 403 So. 2d 1137, 1138 (Fla. 4th DCA 1981); *Zipperer v. City of Fort Myers*, 41 F.3d 619, 623 (11th Cir. 1995). This is because a mortgagee has the right to foreclose and reforeclose its lien, which means that a mortgage is a cause of action creating a lien on the property. *See Head*, 797 So. 2d at 1268 (citing *Zipperer*, 41 F.3d at 623); *United of Fla., Inc. v. Illini Fed. Sav. & Loan Ass'n*, 341 So. 2d 793, 794 (Fla. 2d DCA 1977) (citing *Shavers v. Duval County*, 73 So. 2d 684 (Fla. 1945)); *Zipperer*, 41 F.3d at 623. Causes of action are protected by the Due Process Clause of the United States Constitution's Fourteenth Amendment. *See Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 428 (1982); *Zipperer*, 41 F.3d at 623.

A mortgage is also a contract, and Florida's Constitution prohibits impairment of contracts. *See Dewberry v. Auto-Owners Ins. Co.*, 363 So. 2d 1077, 1079 (Fla. 1978); *Sarasota County v. Andrews*, 573 So. 2d 113, 115 (Fla. 2d DCA1991); *First Nationwide Mort. Corp. v. Brantley*, 851 So. 2d 885, 887-88

(Fla. 4th DCA 2003) (Fleet, A.J., concurring). In Florida, virtually no degree of contract impairment is tolerated. *Andrews*, 573 So. 2d at 115. Any legislative action that diminishes a contract's value is repugnant to the Florida Constitution. *Dewberry*, 363 So. 2d at 1080. Without a doubt, mortgages are constitutionally protected interests.

Allowing Superpriority Lien Status Impairs Contract Rights

Once a mortgage lien is recorded, allowing a later-recorded lien to pass over the earlier-recorded mortgage lien—also known as granting superpriority rights—would trample on the earlier mortgagee's constitutionally protected, vested rights. *See Andrews*, 573 So. 2d at 115; *Coral Lakes Comm. Ass'n, Inc. v. Busey Bank, N.A.*, 30 So. 3d 579, 584 (Fla. 2d DCA 2010) (noting that even statutory change could not allow homeowners' association lien priority over earlier-recorded mortgage because to hold otherwise would implicate constitutional concerns about impairment of vested contractual rights); *cf. Citrus Mem'l Health Found., Inc. v. Citrus County Hosp. Bd.*, 108 So. 3d 675, 678 (Fla. 1st DCA 2013) (finding special law unconstitutional because it altered a party's existing contract, thereby running afoul of Article I, Section 10 of Florida's Constitution).

Thus, a later-recorded loan, even one between a municipality and a property owner in furtherance of stated public policy goals, cannot have superpriority rights against an earlier-recorded mortgage lien. *See Brantley*, 851 So. 2d 885, 887-88

(Fla. 4th DCA 2003) (noting that even if city gave loan for purpose of making improvements in connection with public policy goals, it still could not take priority over purchase money mortgage, and, in concurrence, stating that as to any program where an individual received governmental assistance for property improvement, superpriority lien rights to the government would not pass constitutional muster). In fact, there is no authority in Florida that allows a mere loan to be given superpriority lien status against a purchase money mortgagee.

Andrews further explains why a superpriority provision that applies to existing mortgage contracts offends the United States and Florida Constitutions. 573 So. 2d at 115. The impairment of contract is immediate because the earlier-recorded mortgagee is automatically at a greater risk of losing its investment if it no longer has a first priority lien. *Id.* The contract also loses value because the marketability of the mortgage on the secondary market declines. *Id.*

Given these constitutional concerns, when the Florida Legislature grants superpriority status to certain types of liens, it is careful to exempt earlier-recorded first mortgagees from that superpriority. *See, e.g.,* § 206.15, Fla. Stat. (2014) (allowing superpriority to property liens that result from non-payment of fuel tax with exception for earlier-recorded mortgagees); § 207.015, Fla. Stat. (2014) (allowing superpriority to property tax liens that result from unpaid commercial motor vehicle privileges tax with exception for earlier-recorded mortgagees); §

320.409, Fla. Stat. (2014) (giving superpriority to property tax liens that result from unpaid license taxes with exception for earlier-recorded mortgagees); § 713.77, Fla. Stat. (2014) (giving superpriority to mobile home park owners' liens against occupants with exception for unpaid purchase money mortgagees).

In fact, superpriority rights over a mortgagee are appropriate only when the mortgagee must yield to the sovereign's taxing power with respect to real property, which is why ad valorem taxes and non-ad valorem special assessments may rightly have lien priority over an earlier-recorded mortgage. *See Gailey v. Robertson*, 123 So. 692, 693 (Fla. 1929) (finding that special assessment lien stemming from street paving improvements had priority over earlier-recorded mortgage lien and such superpriority did not impair vested rights of mortgagee because mortgagee must yield to the sovereign's power to impose taxes); *see also Straughn v. Camp*, 293 So. 2d 689, 694 (Fla. 1974) (noting that contract rights are subject to Legislature's taxing power). Absent the use of this taxing authority, a mere loan between a municipality and a citizen cannot be the basis for the municipality to have lien priority over an earlier-recorded mortgage. *See Brantley*, 851 So. 2d at 887.

Turning to the case at hand, Florida's PACE Act, found at section 163.08, Florida Statutes, unconstitutionally grants superpriority lien status to the liens that arise when the FDFC loans money to a property owner to finance qualifying

improvements. The Florida Legislature has couched repayment of these PACE loans as "non-ad valorem special assessments" in an effort to justify the superpriority status it has given the resulting liens. In reality, though, these repayments are not special assessments; they are nothing more than standard loan repayments. The borrower is the property owner, and the lender is the FDFC.

Below, we show why that method of repayment by a property owner is a loan payment rather than the payment of a non-ad valorem special assessment. And, because it is only a loan payment, superpriority against earlier-recorded mortgagees is prohibited. *See Brantley*, 851 So. 2d at 887. Thus, when the Florida Legislature granted superpriority lien status for PACE loans, it infringed on the constitutionally protected rights of mortgagees around the state of the Florida.[2]

The PACE Loan Payments Are Not Non-Ad Valorem Special Assessments

To understand why the PACE Act's method of loan repayment is not actually a non-ad valorem special assessment requires a general discussion about what constitutes a special assessment and what does not. When determining

[2] Even worse, when the Legislature gave this superpriority lien status, it was not protecting the government (which, as *Brantley* shows, is not enough for superpriority lien rights over a purchase money mortgagee), but a private corporation. In fact, the entity that will really benefit from this superpriority lien status is Renovate America, Inc., the company that first created the title "HERO Program," that will administer Florida's HERO Program, and that will then become, due to the PACE Act's superpriority lien rights, the virtually risk-free investor in the HERO Program because it will be the holder of all of the issued bonds. And it is just a private corporation like any bank.

whether a payment by a property owner is a special assessment, the fact that the government has titled the payment an "assessment" is not controlling. *See City of Gainesville*, 863 So. 2d at 144 (citing 70C Am. Jur. 2d, *Special or Local Assessments* § 2, at 631-32 (2000)).

Generally, a special assessment is a "charge assessed against property of some particular locality because that property derives some special benefit for the expenditure of the money." *Workman Enters., Inc. v. Hernando County*, 790 So. 2d 598, 599 (Fla. 5th DCA 2001) (quoting *Atl. Coast Line R.R. Co. v. City of Gainesville*, 91 So. 118 (Fla. 1922)). Thus, for an assessment to be valid, an assessed property must derive a special benefit from the service provided, and the assessment must be fairly and reasonably apportioned according to the benefits received. *Id.* (citing *Sarasota County v. Sarasota Church of Christ, Inc.*, 667 So. 2d 180, 183 (Fla. 1995)). Examples of improvements that result in valid non-ad valorem special assessments include paving a subdivision's streets or putting in sidewalks. *See, e.g., State v. Sarasota County*, 693 So. 2d 546, 548 (Fla. 1997) (validating bonds related to special assessment for stormwater runoff and determining that assessment was, in fact, an assessment rather than a tax); 1B Matthews Municipal Ordinances § 36:2 (2d ed.).

Thus, even if a special assessment provides a special benefit to property, that special benefit must still be public. That is to say, it is a benefit to a group of

properties within a community, usually for improvements that specially benefit that group, of the type described above, such as road, sidewalk, street lighting, and other local improvements. A special assessment is not a special benefit to an individual property. *See Atl. Coast Line R.R. Co. v. City of Lakeland*, 115 So. 669, 684 (Fla. 1927) (Strum, J., concurring) ("The purpose for which [an] assessment is imposed must, of course, be public in its nature as distinguished from one designed solely for private benefit."); *see also* § 170.01, Fla. Stat. (2014) (authorizing municipalities to levy special assessments to pay for public improvements such as road and sewer construction and repair, utilities relocation, public park construction, wetlands drainage, and mass transportation systems); 1B Matthews Municipal Ordinances § 36:2 (2d ed.) (describing typical projects that are the subject of financing through special assessments).

A key distinction between a special assessment and other government-imposed payments by a property owner, such as user fees, is the voluntary nature of the payment. Unlike other payments by property owners, but like taxes, special assessments are mandatory, not voluntary. *See City of Boca Raton v. State*, 595 So. 2d 25, 29 (Fla. 1992) ("Taxes and special assessments are distinguishable in that, while both are mandatory, there is no requirement that taxes provide any specific benefit to the property. . ."); *Klemm v. Davenport*, 129 So. 904, 907 (Fla. 1930) ("A 'special assessment' is like a tax in that it is an enforced contribution

from the property owner . . ."); Henry Kenza Van Assenderp, *Dispelling the Myths: Florida's Non-Ad Valorem Special Assessments Law*, 20 Fla. St. U. L. Rev. 823, 826 (1993) ("[N]on-ad valorem special assessments are compulsory levies of local government.").

This issue of voluntariness is illustrated in Florida's common law through a review of cases where special assessments are compared to user fees—the two types of payments are often considered similar under the law because both provide a special benefit to the property being charged. *See City of Gainesville*, 863 So. 2d at 144. User fees are "charges based upon the proprietary right of the government body permitting the use of the instrumentality involved." *Gargano v. Lee County Bd. of County Comm'rs*, 921 So. 2d 661, 667 (Fla. 2d DCA 2006) (quoting *City of Port Orange*, 650 So. 2d at 3). Like special assessments, user fees provide special benefits to the party paying the fee. *Id.* As a result of the similarity between user fees and special assessment and to illustrate the nature of a special assessment, we will touch upon some of the cases discussing what makes a particular government charge to a property owner a special assessment versus a user fee.

One of the main ways that user fees and special assessments are dissimilar is that user fees are paid by choice; that is, they are voluntary. *City of Gainesville*, 863 So. 2d at 144. Unlike a special assessment, a property owner can avoid the charge by choosing not to take part in the government service being offered. *Id.*

Thus, comparing user fees and special assessments to ad valorem taxes, user fees are unlike taxes because they are usually voluntary instead of compulsory; special assessments, on the other hand, are always compulsory. *City of Port Orange*, 650 So. 2d at 3 ("[User] fees share common traits that distinguish them from taxes: they are charged in exchange for a particular government service which benefits the party paying the fee in a manner not shared by other members of society, and they are paid by choice, in that the party paying the fee has the option of not utilizing the government service and thereby avoiding the charge."); *see also City of Boca Raton*, 595 So. 2d at 29 (comparing and contrasting taxes and special assessments).

For example, in *City of Gainesville*, this Court found the City's stormwater charges were user fees, not special assessments. 863 So. 2d at 140. In grappling with the issue of whether the charges were fees or assessments, one reason this Court determined that the charges were fees related to the voluntary nature of the charges. *Id.* at 146. While the State argued that the stormwater system charges were special assessments, this Court disagreed, finding that the payments were voluntary fees. *Id.* The City required that only properties that actually used the stormwater system had to pay the fee. *Id.* Thus, property owners could avoid the fee by either not developing the property or by implementing a system to retain stormwater on site. *Id.* The charge was also voluntary as to tenants of property

owners because the tenants could avoid the charge by choosing to live on properties that did not use the City's stormwater system. *Id.*

Similarly, in *Okeechobee Utility Authority v. Kampgrounds of America, Inc.*, the Fourth District had to decide whether the method the Okeechobee Utility Authority used for imposing charges against a number of campground facilities constituted assessments or fees. 882 So. 2d 445, 446 (Fla. 4th DCA 2004). The court found that the charges were user fees, in part due to the voluntary nature of the charges—they were imposed against only those opting to connect to the utility lines, and the property owner could avoid the charge by refusing the service. *Id.* at 447. Thus, the charges were not special assessments.

In a comparable case, which did not involve special assessments, but did involve whether a reclaimed water charge was a user fee or a tax, this Court found the charge a user fee, stating, "there is no question that the Availability Charge provides a special benefit to those paying the fee . . . Rather than going into the general revenue fund, the money which is recouped through the Availability Charge is tied directly to payment for . . . the improvements extending to the individual properties . . . and collection of the charge ceases when those costs have been recovered." *Pinellas County v. State*, 776 So. 2d 262, 267 (Fla. 2001).

What the foregoing cases show is that, in Florida, a special assessment is never voluntary. Any government-imposed charge against a property owner that is

voluntary must be a user fee or some other type of charge; it cannot be a special assessment or an ad valorem tax. Additionally, a special assessment is not for an improvement to a particular and distinct piece of property; it is for an improvement that will specially benefit only some properties in a community, but the improvement is still public in nature.

In this case, under Florida's PACE Act, the FDFC is not levying "non-ad valorem special assessments." First, the so-called assessment is purely voluntary. It is assessed only if a property owner takes the affirmative action of applying for funds from the FDFC. § 163.08(4), Fla. Stat. Thus, the only property owners who will ever pay this "assessment" do so because they signed up for it. Second, the charge being levied by the FDFC is for an improvement that specially benefits a lone lot or piece of property. The improvement is not public in nature. It is not a sidewalk or street light or sewer main or wetlands drainage or the like. Instead, it is an improvement that is unique and distinct and made on a piecemeal, per-property basis.

For these reasons, the "non-ad valorem special assessments" discussed in section 163.08 are merely loan repayments between the FDFC and individual property owners, and nothing more. Like any other loan, the property owner applies for financing, and once approved, receives the financing and uses it for the improvements. Then over time, the property owner has to repay the financing.

Here, the lender is simply the FDFC instead of a private lending institution. Even Renovate America, Inc., the private entity that will be administering Florida's HERO Program under the PACE Act (and the company that coined the title "HERO Program"), refers to the PACE loans as "loans," and despite the PACE Act's statutory "credit check" on borrowers, touts loan approvals within thirty seconds. *See* Who We Are, http://renovateamerica.com/about, and The Award Winning HERO Program, http://renovateamerica.com/hero-program (last visited October 6, 2014).

Indeed, Florida courts have expressly found that such loans like the PACE loans are not non-ad valorem special assessments. This is illustrated in *Brantley*, a case involving a program very similar to the FDFC's HERO Program here. 851 So. 2d 885.

In *Brantley*, the City of Lauderdale Lakes instituted a Home Investment Partnership Program pursuant to the Community Redevelopment Act of 1969, which was a program whereby the City loaned funds to property owners for the purpose of making improvements to the property. *Id.* at 886-87. Four years earlier, before entering into a financing agreement with the City for improvements, Brantley had executed a purchase money mortgage in favor of First Nationwide. *Id.* at 886. Brantley defaulted on her mortgage, and First Nationwide brought a foreclosure action. *Id.* The City responded to the action, arguing that its lien was

superior to First Nationwide's because the City's loan to Brantley was part of community redevelopment and related services. *Id.* at 887. The City further relied on its Code of Ordinances, which provided that "[e]ach and every municipal lien existing from the delivery of municipal services, including liens for special assessments . . . shall be deemed to be prior in dignity to any other lien, including mortgages, irrespective of the date of the recording of the municipal lien or the date of recording of any mortgage . . ." *Id.*

The appellate court reversed the trial court's summary judgment that favored the City, finding that although the City's loan to Brantley was provided in connection with the Home Investment Partnership Program, it was nonetheless given for the sole purpose of making home repairs. *Id.* That did not qualify as a lien resulting from municipal services or special assessments, and the City's lien could not take priority over First Nationwide's purchase money mortgage. *Id.*

The facts of *Brantley* are similar to those at hand. The Home Investment Partnership Program established under the Community Redevelopment Act at issue in *Brantley* is not unlike the HERO Program established under the PACE Act. The only difference is that, in the PACE Act, the loan repayment is termed a "special assessment." Beyond that, the programs are quite similar. In each instance, to encourage property owners to make improvements to their property, the local government is lending funds to those property owners. And, in both cases—

Brantley and now, under the PACE Act—the respective programs attempted to provide their liens with priority over previously-recorded purchase money mortgages.

Because the PACE Act's Loan Repayment is Not a "Non-Ad Valorem Special Assessment," the Superpriority Lien Rights Given By the PACE Act Render the Act Unconstitutional

As illustrated above, the PACE Act loan repayments are not actually special assessments. Accordingly, the PACE Act liens do not fall into the small category of liens—those imposed as part of the state's taxing authority—that can have superpriority over a mortgagee's earlier-recorded lien without impairing that mortgagee's constitutional rights.

The PACE Act simply provides individual loans for individual property improvements. The PACE Act itself essentially acknowledges this fact, stating that the Act will "enabl[e] property owners to *voluntarily* finance such improvements with local government assistance." § 163.08(1)(b), Fla. Stat. (emphasis added). As in *Brantley*, although the improvements are made pursuant to the HERO Program, they remain nothing more than updates and repairs to individual properties.

Ultimately, even if the property improvement programs are based on legitimate state public policy goals and interests—whether those goals be remedying slum and blighted areas (like *Brantley*), or here, energy efficiency and

conservation along with hurricane mitigation—constitutionally protected rights of mortgagees cannot be crushed by government loan programs. As Judge Fleet stated in *Brantley*:

> While laudable in its goal, the Community Redevelopment Act of 1969 must still comport with fundamental constitutional requirements. Article I, Section 10 of the United States Constitution and Article I, Section 10 of Florida's Declaration of rights each specifically prohibit governmental bodies from enacting any law which impairs the obligation of contract. To accept the proposition that governmental assistance to an individual, natural or corporate, for residential improvement automatically becomes superior in dignity to a previously recorded mortgage simply fails to pass constitutional muster.

851 So. 2d at 887-88 (Fleet, A.J., concurring).

Similarly, the PACE Act's goals are laudable. As the Legislature found, energy-related improvements should assist in reaching the state's goal of lower energy consumption. However, the state cannot work toward that goal by overriding private constitutional rights. The Florida Legislature can hinder a mortgagee's constitutional property and contract rights only upon passage of a valid assessment or tax under the state's taxing authority, which has not happened here. *See Gailey*, 123 So. at 693.

This Constitutional Infringement is Causing Real World Problems

The devastating impact of the PACE Act's constitutional infringement cannot be overstated. Banks are highly regulated entities. A primary concern for regulators is whether banks are adequately capitalized. One of the significant

factors in that analysis is whether the loans extended by a bank are backed by sufficient collateral to make the bank whole if a borrower defaults on the loans. The bank necessarily performs its analysis of the loan collateral at the time the loan is made and as a result, builds terms into the mortgage and/or note agreement that allow the bank to take action if the collateral becomes insufficient. The PACE Act strips this protection from the mortgage contract, thus unconstitutionally impairing the contract, while at the same time allowing loans that could encumber the property beyond its fair market value. *See* § 163.08(12)-(13), Fla. Stat.

Because the PACE loans affect the collateralization of existing mortgages, the safety and soundness of banks are at issue given that their existing loans will fall into second position and, on top of that, are potentially under-collateralized. This is because PACE loans have superpriority lien rights and can encumber the property in an amount up to 20% of the property's appraised value. *See* § 163.08(8) & (12), Fla. Stat. As a result, a prudent regulator would require a bank considering a seemingly first position purchase money mortgage to loan against only 80% of the appraised value of the property. *Cf., e.g.,* Federal Deposit Insurance Corporation, https://www.fdic.gov/regulations/safety/manual/ (follow "3.1 Asset Quality" hyperlink) ("Asset quality is one of the most critical areas in determining the overall condition of a bank. The primary factor affecting overall asset quality is the quality of the loan portfolio and the credit administration

program. Loans typically comprise a majority of a bank's assets and carry the greatest amount of risk to their capital."). Such a situation limits the availability of credit, which is detrimental to the growth and development of a state whose economy is still struggling toward recovery.

Florida has had one of the highest rates of bank failures in the country since 2008—71 institutions failed between 2008 and 2014—in large part because of the real estate market collapse. *See* Federal Deposit Insurance Corporation, https://www2.fdic.gov/hsob/ (follow "Failures & Assistance Transactions" hyperlink; then sort by "Florida" from 2008 to 2014). In the face of that, the Florida Legislature has put banks in an untenable situation because it has placed the burden of PACE loans on mortgagees that, as a result of the Act, are no longer able to properly analyze the soundness and security of a loan.

Moreover, the impact of this unconstitutional statute is not limited to banks. While the Florida Bankers Association's constituents are lenders whose constitutional rights are at issue, the PACE Act also negatively affects lending generally and the ability of non-prime borrowers to obtain mortgages.

Specifically, the Federal Housing Finance Agency ("FHFA") has asked states to reconsider PACE programs particularly as to those programs that allow PACE loans to acquire a priority lien over existing mortgages. Federal Housing Finance Agency, FHFA Statement on Certain Energy Retrofit Loan Programs

(2010), http://www.fhfa.gov/Media/PublicAffairs/Pages/FHFA-Statement-on-Certain-Energy-Retrofit-Loan-Programs.aspx. According to the FHFA the problem with this lien superpriority is that "[f]irst 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." *Id.* In essence, what the FHFA has noted is exactly what we argued above—these PACE liens stem from pure loans without any of the hallmarks and community benefits of a true non-ad valorem special assessment.

Furthermore, the FHFA has determined that PACE programs that afford superpriority rights alter traditional lending priorities, thereby disrupting a healing, still-fragile housing market. *Id.* This means a lack of solid underwriting standards to protect homeowners and a lack of consumer protection standards to assist property owners and lenders in evaluating the value of energy retrofit products. *See id.* Ultimately, the FHFA has found that PACE programs allowing for superiority of PACE loans present risk to lenders and secondary market entities, may alter valuations for mortgage-backed securities, and are not essential for successful energy conservation programs. *Id.*

As a result of these concerns, the FHFA directed Fannie Mae, Freddie Mac, and the Federal Home Loan Banks to undertake certain prudential actions. *Id.* Those actions included, but were not limited to: adjusting loan-to-value ratios to reflect the maximum permissible PACE loan amount available to borrowers in PACE states; ensuring that loan covenants require approval or consent for any PACE loan (although Florida's PACE Act does not allow such lender carte blanche); and tightening borrower debt-to-income ratios to account for additional obligations associated with possible future PACE loans. *Id.*

After this FHFA directive, sure enough, less than two months ago, Freddie Mac published an industry letter concerning its position that mortgages secured by properties with an outstanding PACE or PACE-like obligation are ineligible for purchase. Industry Letter from Freddie Mac to Freddie Mac Sellers and Servicers, Subject: Mortgages Secured by Properties with an Outstanding Property Assessed Clean Energy (PACE) or Pace-like Obligation Ineligible for Purchase (2014), http://www.freddiemac.com/singlefamily/guide/bulletins/pdf/iltr082014.pdf. The letter referenced the FHFA's finding that PACE programs that permit lien priority over existing mortgage liens pose unusual challenges and change customary lender priorities. *Id.* Thus, with only one exception, Freddie Mac will not purchase either purchase transaction or refinance mortgages subject to PACE obligations that

allow for superpriority. *Id.* Freddie Mac may take additional action as necessary to mitigate greater risks associated with PACE programs. *Id.*

What this shows is that Florida's PACE Act, while based on admirable aspirations, is actually fraught with problems for the housing market and borrowers, all as a result of changing longstanding lending practices. Some of the very problems highlighted by the FHFA go to the constitutional issues we have already discussed.

Because the PACE Act's Financing System is Unconstitutional, the FDFC Does Not Have Authority to Issue the Bonds, and Bond Validation is Inappropriate

As we have shown, the method of repayment of the PACE loans—by charging so-called voluntary "non-ad valorem special assessments"—is unconstitutional. No PACE loan repayment can ever be a true "special assessment," and thus the Act will always be facially unconstitutional. *See Fla. Dep't of Revenue v. City of Gainesville*, 918 So. 2d 250, 256 (Fla. 2005) (noting that when no circumstances exist under which statute would be valid, it is facially unconstitutional).

This unconstitutional method of loan repayment is the financing arrangement by which the revenue bonds the FDFC wants to issue are secured. § 163.08(4), Fla. Stat. Because the financing agreement for securing the bonds is unconstitutional, the FDFC does not have the authority to issue the bonds in

dispute. *City of Gainesville*, 863 So. 2d at 143 (explaining that, in a bond validation appeal, part of the inquiry as to whether public body has authority to issue bonds is the legality of the financing agreement upon which the bond is secured). As a result, the bonds cannot be validated, and this Court should reverse.

CONCLUSION

In a bond validation case, this Court considers whether a public body has the authority to issue the bonds in dispute. Part of that inquiry is the legality of the financing agreement upon which the bonds are secured. Here, the bonds are secured by non-ad valorem special assessments. This financing arrangement is illegal and must fail because the non-ad valorem special assessments are not truly special assessments, but instead, loan repayments. Allowing mere loan repayments superpriority lien rights over earlier-recorded mortgage liens is always unconstitutional. As a result, the financing agreement securing the bonds is illegal, and thus the FDFC does not have the authority to issue the bonds. The bonds cannot be validated, and this Court should reverse.

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CERTIFICATE OF COMPLIANCE

I HEREBY CERTIFY that this brief complies with the font requirements of Florida Rules of Appellate Procedure 9.210(a)(2).

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