

Overview of April Guide Updates and Other Process Changes

April 12, 2024



Agenda



- Purpose of this training
- Guide updates/process changes effective 4/18/2024
 - New Categories of Key Borrower Principals
 - Enhanced Due Diligence
 - Inspection/Lease audit
 - Web Search Tool
 - Appraiser Independence Requirements/Appraisal review
 - Restricted Vendor List and Title Companies
- Questions



Purpose of this Training (*The “Why”*)

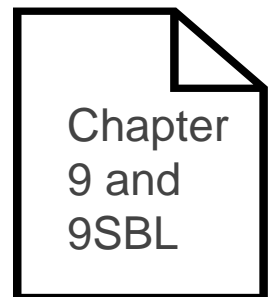
- Heads up on process changes that will be introduced with the Guide update scheduled for 4/18/2024
- Focus of the changes:
 - Strengthen due diligence activities, primarily around KYC
 - Enhance fraud detection efforts
 - Mitigate credit risk

This deck is intended as an overview only and is not meant to replace or supersede anything contained within the Guide update itself.

Introduction of New Categories of KBP Types



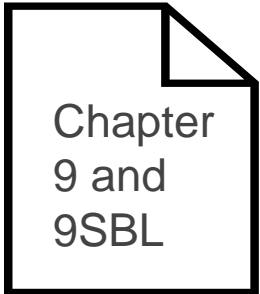
- In support of our commitment to strengthening Know Your Customer (KYC) activities, **a risk-based approach to enhanced due diligence** activities will apply to Key Borrower Principals (KBP) who are either:
 - In a position of **Ultimate Control** (or pre-approved to take over Ultimate Control via buy-sell) or
 - **Guarantors**



Introduction of New Categories of KBP Types

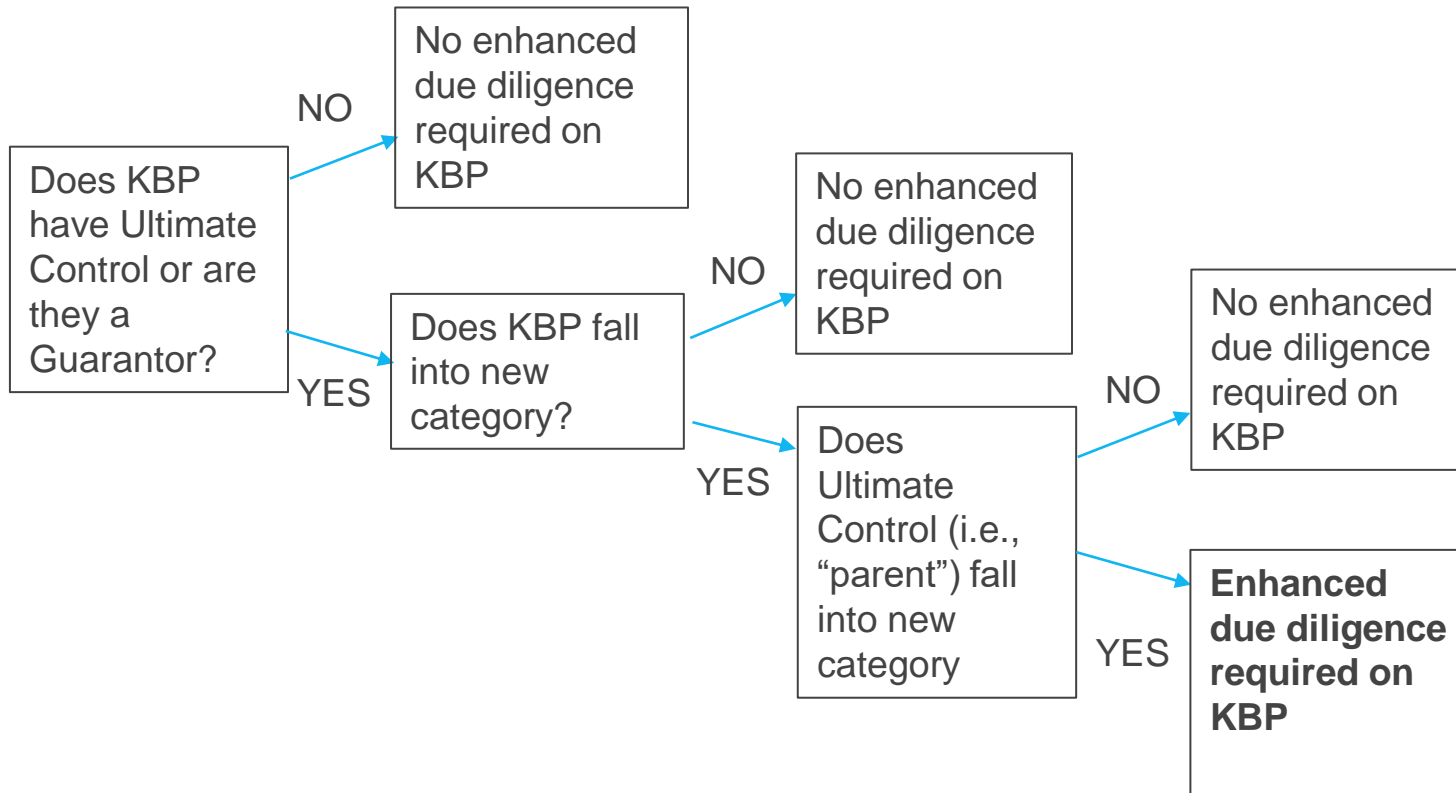


- Applicable KBPs may now fall into **two new categories** used to determine when enhanced due diligence is required:
 - **First-Time Sponsor** – When neither the KBP nor its Ultimate Control has transacted multifamily business with Freddie Mac in the past 10 years
 - **Limited Multifamily Experience Sponsor** –
 - For non-SBL, when neither the KBP nor its Ultimate Control has had Control of at least 5 properties in the past 5 years, the majority of which are or were substantially similar to the Property (e.g., number of units or type of property)
 - For SBL, **no change** to the current “Borrower Experience Baseline” requirements (including tighter credit parameters and prescreen)

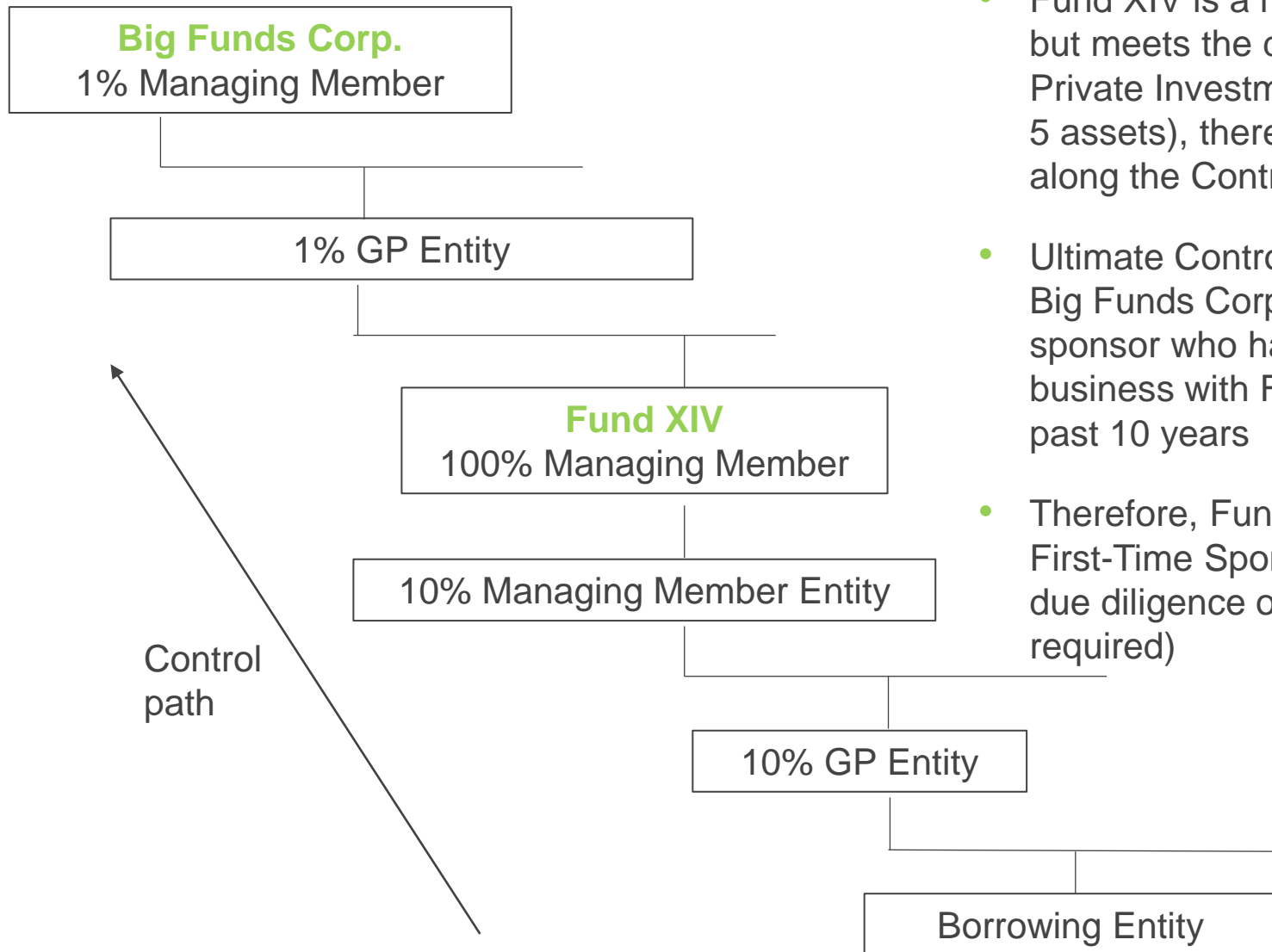
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Introduction of New Categories of KBP Types (cont'd)

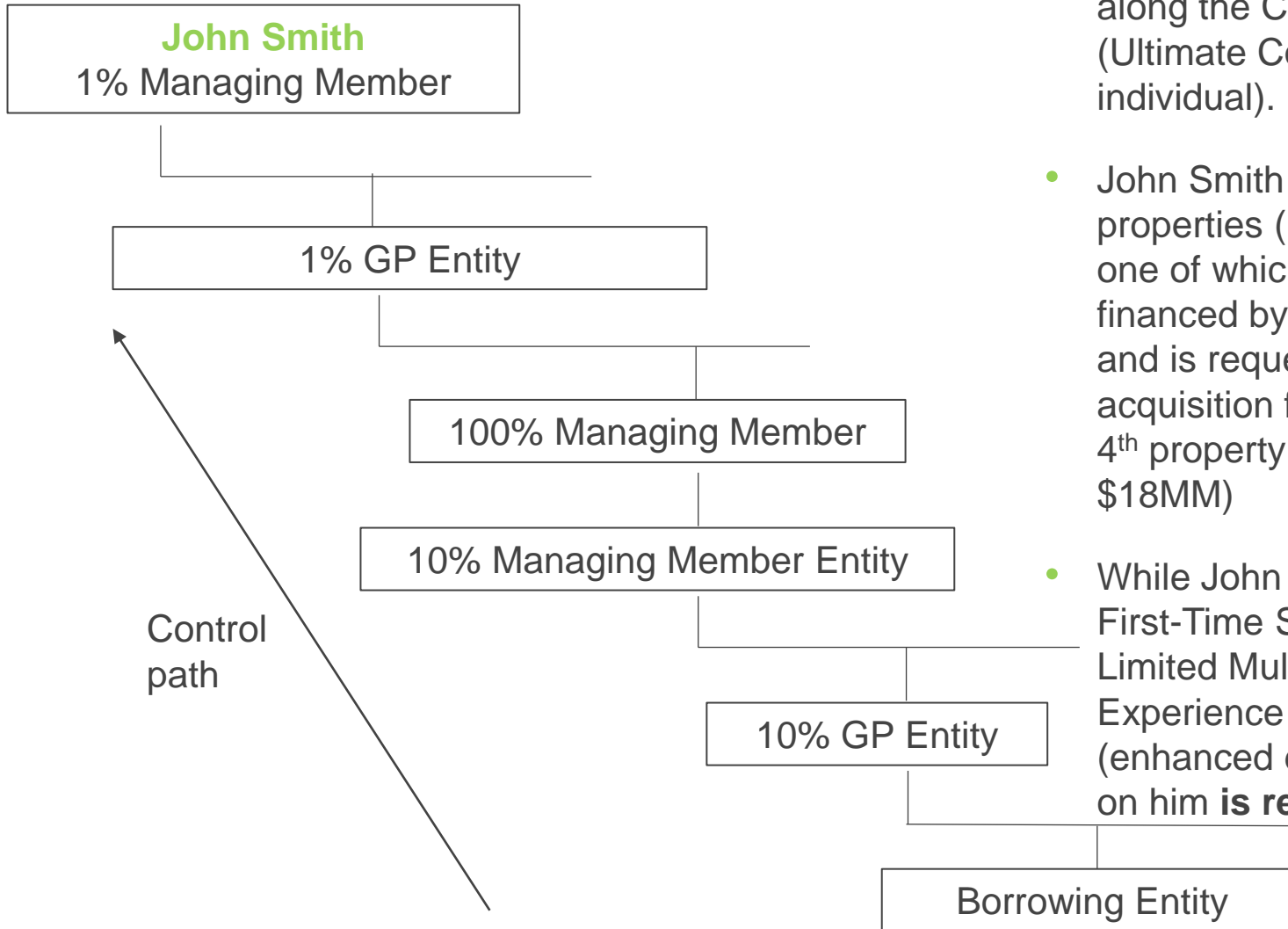


Introduction of New Categories of KBP Types (cont'd)



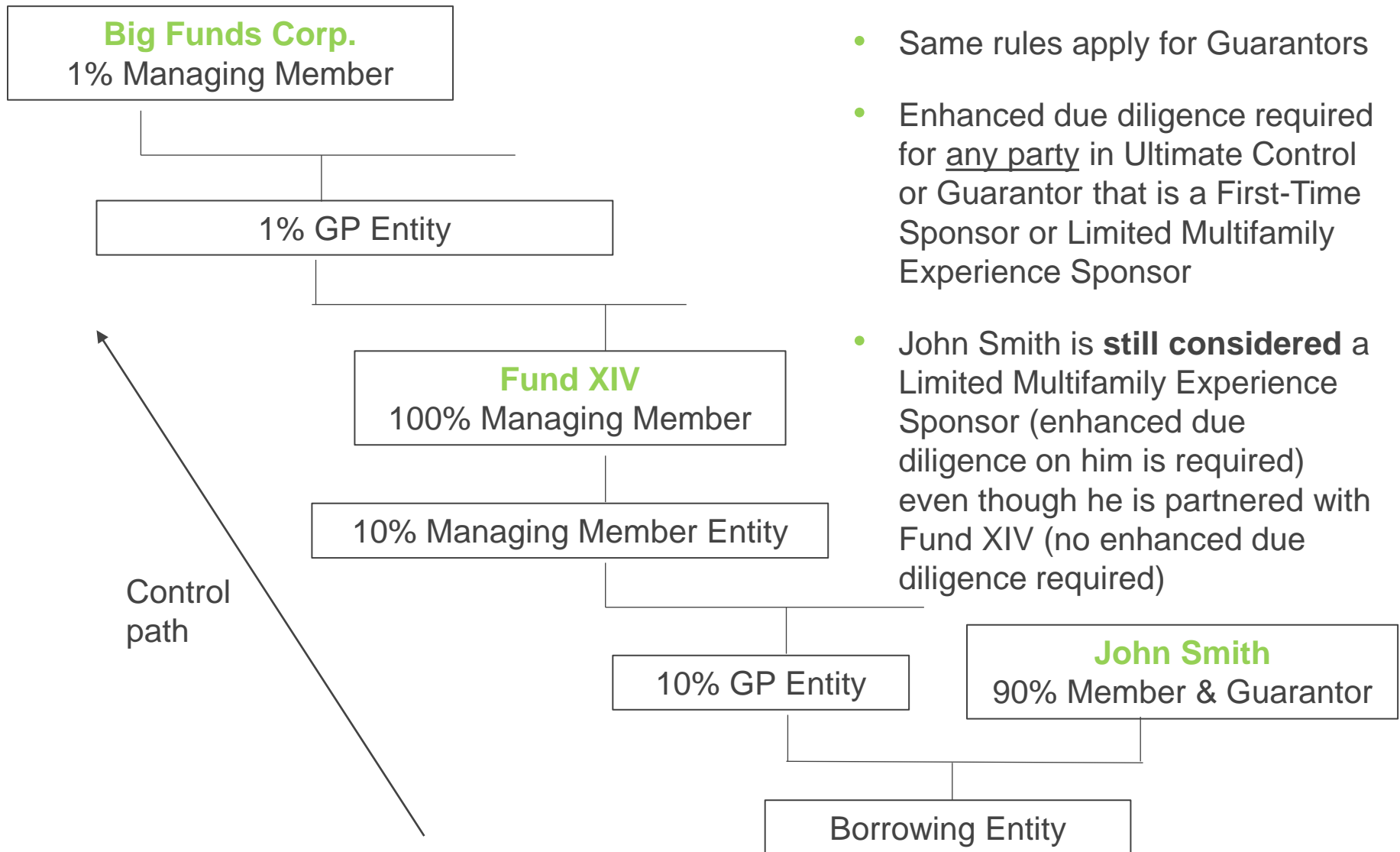
- Fund XIV is a new fund to FM, but meets the definition of Private Investment Fund (has > 5 assets), therefore it is the KBP along the Control path
- Ultimate Control of Fund XIV – Big Funds Corp. – is a repeat sponsor who has transacted business with Freddie Mac in the past 10 years
- Therefore, Fund XIV is **not** a First-Time Sponsor (enhanced due diligence on this fund is not required)

Introduction of New Categories of KBP Types (cont'd)



- John Smith is the KBP along the Control path (Ultimate Control and an individual).
- John Smith owns 3 MF properties (100- 200 units), one of which was recently financed by Freddie Mac, and is requesting FM acquisition financing for a 4th property (225 units, \$18MM)
- While John Smith is not a First-Time Sponsor, he **is** a Limited Multifamily Experience Sponsor (enhanced due diligence on him **is required**)

Introduction of New Categories of KBP Types (cont'd)

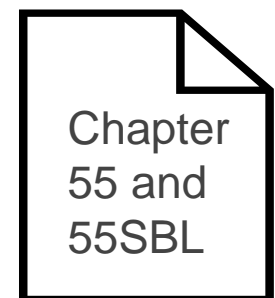
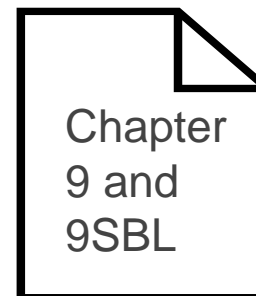


- Same rules apply for Guarantors
- Enhanced due diligence required for any party in Ultimate Control or Guarantor that is a First-Time Sponsor or Limited Multifamily Experience Sponsor
- John Smith is **still considered** a Limited Multifamily Experience Sponsor (enhanced due diligence on him is required) even though he is partnered with Fund XIV (no enhanced due diligence required)

Disclosure of New Categories of KBP Types

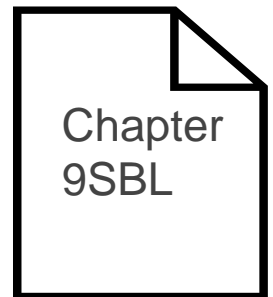


- At Quote – if questions about whether a certain party meets the definition of a KBP type that would require enhanced due diligence, discuss with Producer
- At Underwriting -
 - Mortgage Transaction Narrative Analysis (Guide Section 55.2 and 55SBL.2) requirements will be updated to require disclosure if KBP meets criteria for First-Time Sponsor or Limited Multifamily Experience Sponsor
 - Review SREO to help identify applicable sponsors



Program-specific impacts of New Categories of KBP Types

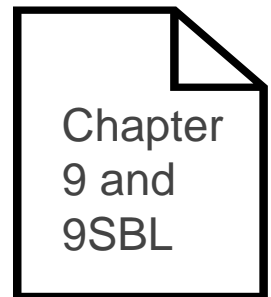
- A few **SBL** reminders:
 - No changes to the current Borrower Experience Baseline requirements
 - The Borrower/Key Borrower Principal due diligence and geographic proximity requirements for Very Small Markets (Guide Section 9SBL.14) will no longer be in effect (replaced by the updated requirements)
- Experience requirements for certain types of products (i.e., Student, MHC, Seniors, etc.) **remain unchanged**



Enhanced Due Diligence Requirements – Overview



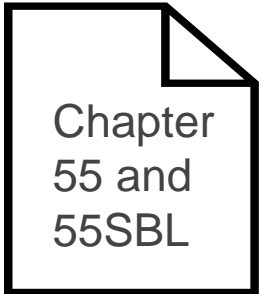
- For KBPs in position of Ultimate Control or Guarantor identified as a First-Time Sponsor or Limited Multifamily Experience Sponsor, additional enhanced due diligence is required:
 - **Liquidity verification** – to verify the liquidity represented in the KBP’s certified financial statement
 - **SREO verification** – to confirm that the KBP has accurately represented their ownership and role in the assets listed in the schedule:



Enhanced Due Diligence Requirements – Liquidity Verification



- Bank or brokerage statements must be submitted as part of the full underwriting package and uploaded to DMS under the “Financial Statement” Document Type with the appropriate Title
- Must be dated within 60 days of the submission of the full underwriting package
- Not applicable to U.S. publicly traded companies
- For Private Investment Funds meeting these criteria, additional documentation acceptable to FM must be provided to support unfunded capital commitments (i.e., investor subscription agreements or similar documentation) but **we cannot rely solely upon** a certification from the Borrower or KBP

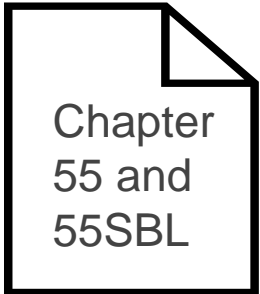
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Enhanced Due Diligence Requirements – Liquidity Verification



- Purpose is to verify the liquidity represented on the certified financial statement
- Deviations need to be thoroughly explained in the Mortgage Transaction Narrative Analysis
 - Timing issues with statements
 - Still a path forward
 - Potential to trigger a higher approval level or additional level of review

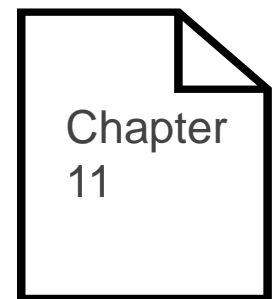
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Enhanced Due Diligence Requirements – SREO Verification



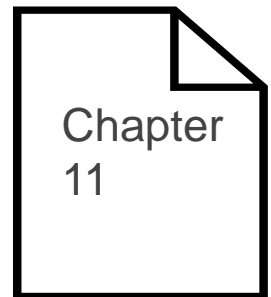
- Purpose is to confirm that the ownership (including the role) is accurately reflected
- Must be completed prior to the submission of the Form 1116/ SREO schedule with the full underwriting package
- By submitting the real estate schedule, Lender certifies that it has completed this validation



Enhanced Due Diligence Requirements – SREO Verification



- Lender completes the validation by performing the following two steps (Guide requirement):
 1. Confirm the owner name of each asset (i.e., a tax bill, title policy, etc.)
 2. Review organizational documents for each owner (redacted copies acceptable) to verify ownership and role of applicable KBP
- Other methodologies **must be approved by Freddie Mac prior to submission** of the Form 1116/ SREO schedule
 - Federal tax return listing assets owned
 - Website listing real estate assets for an SEC-registered entity
 - Certification from Lender involved in the financing of certain assets
- Supporting documentation is not required to be submitted in the full underwriting package but must be retained by the Lender



Inspection Requirement Changes



- Increased sample size of unit inspections:

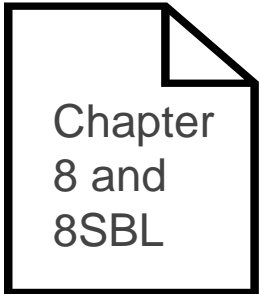
Core:

Unit inspection sample size increasing to **10% of units**, with a minimum of **10 units** and a maximum of **30 units**

SBL:

Unit inspection sample size increasing to **10% of units**, with a minimum of **5 units**

- Optigo Happy[®] and Excel inspection and Lease audit template on [Freddiemac.com](https://www.freddiemac.com) will be updated by 4/18/2024

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Inspection Documentation Update



- New look to the Repair & Maintenance section
 - More detailed questions around Material Property Condition Issues

Repairs & Maintenance (R&M) / Material Property Condition Issues

Key: 1. Like New 2. Above Average 3. Average 4. Deteriorating 5. Poor

Enter details...

Site ⓘ

1 2 3 4 5

Status

Enter details...

Selection Required

Concern Identified: Site (trip hazards, asphalt deterioration, etc.)

Y N

Yes / No

Enter details...

Selection Required

Concern Identified: Landscaping/drainage (erosion, ponding, retaining wall condition, overgrown trees, missing gutters/downspouts, etc.)

Y N

Yes / No

Enter details...

Lease Audit Requirement Changes



- Increased **number** of audited leases required:

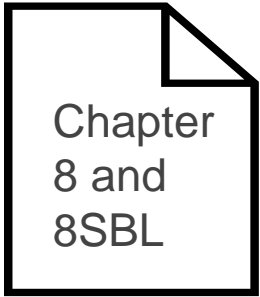
Core:

Lease audit sample size increasing to **10% of units**, with a minimum of **10 units** and a maximum of **30 units**

SBL:

Properties > 15 units - Lease audit sample size the greater of 25% of units or 10 units, with a maximum of **30 units**

Properties ≤ 15 units – Lease audit of 100% of leases, with a maximum of 10 units

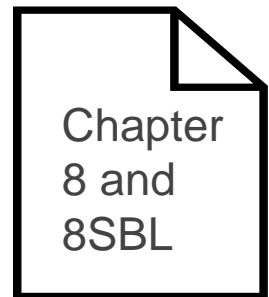
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Lease Audit Requirement Changes (cont'd)



- Additional **validation** must also be performed against documentation reflecting actual rental payments received by the tenant, such as a tenant ledger, general ledger, copies of checks, etc.
 - Comment field available if inconsistencies are noted that require additional explanation
 - Lenders must retain the documentation, but not required to be submitted in the full underwriting package
- Optigo Happy and Excel inspection and Lease audit template on freddiemac.com will be updated by 4/18/2024 to reflect a new space for the additional source document to review





Updated Web Search Tool

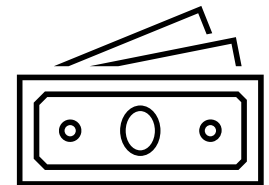
- New Web Search Word document has been updated to contain 5 new words in the search string for owners and property managers (fraud, charge, guilt, embezzle, and sanction)
- External version will also be posted to freddiemac.com for use on 4/18/2024



Enhanced Purchase & Sale Agreement Analysis



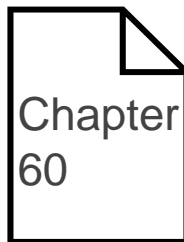
- New form has been available on [freddiemac.com](https://www.freddiemac.com) since 3/26/2024
- Purpose is to do a deeper dive into the parties involved with the acquisition so that we can better understand the transaction to determine if there is any additional credit risk
 - Additional confirmation that the names of various parties in the PSA are consistent with the organizational chart and organizational documents, as applicable
 - Identification of any common ownership/affiliation between the seller and purchaser (based on review of PSA and Borrower confirmation)
 - For real property acquisitions – Confirmation that the Seller is the current owner of the property and when it acquired the property
 - For ownership interest acquisitions – Identification of any prior transfers and the date of the most recent transfer, if applicable





Appraiser Independence Requirements

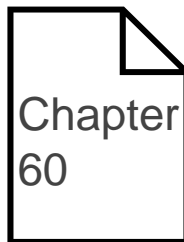
- Intended to safeguard the independence, objectivity and impartiality of appraisers
- General requirements ensure that the valuation process is not directed or influenced in any way by lenders or those acting on lender's behalf, who may not:
 - Provide or suggest an anticipated, encouraged, or desired value or value range for the Property, except for a sales contract
 - Provide or suggest an anticipated, estimated, encouraged, or desired targeted loan ratio (i.e., DCR, LTV, etc.), expense conclusions, or income conclusions
 - Provide comparable sales prior to engaging the Independent Party to perform an Appraisal
 - Threaten to withhold future business or terminate relationship due to a value conclusion being below a lender or borrower's expectation
 - Direct a scope of work contrary to what the appraiser has deemed necessary to produce credible results



Appraiser Independence Requirements (cont'd)



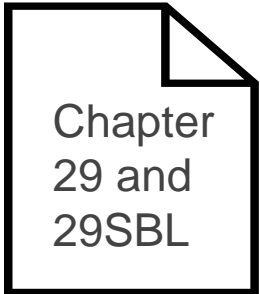
- Additional requirements to ensure appraisal independence
 - Employees of Seller/Service provider involved in the sales or mortgage origination function must not also be involved in the appraisal ordering and review function
 - Seller/Service provider must demonstrate within its written policies that it has prudent safeguards in place to prevent influence or interference
- Seller/Service provider must adopt written policies, procedures and disciplinary rules and implement adequate training programs to ensure compliance with these requirements



Expansion of Restricted Vendor List



- Currently, Lenders must **check the Restricted Vendor List for every loan**
- Multifamily Restricted Vendor List is being expanded to also include **title companies**, when applicable
 - Currently there are no title companies on the list, but there may be in the future
- Lenders must notify us if they have discontinued the use of a title company in connection with any transaction

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Effective Dates

Effective for transactions taken under application on or after 4/18/2024

- Enhanced Due Diligence for First-Time/ Limited Multifamily Experience Sponsors
- Lease audit validation to the tenant ledger

Effective on 4/18/2024 with the Guide Bulletin updates

- Appraiser Independence Requirements
- Expansion of Restricted Vendor List to cover Title Companies
- Inspection and Lease audit sample changes (for inspections not yet completed)



What next?

- Review applicable Guide chapters for more details
- Quote stipulations added ~ 4/12/2024 as a reminder about the new enhanced due diligence requirements
- Process questions can be addressed to Production and Underwriting Teams
- Feedback on process enhancements should first go through your leadership teams

Access the recorded training on Optigo Academy

[Click this link to access the recording](#)



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