



## Moderate Rehab Best Practices: Servicing, Renovation Monitoring, and Draws

The purpose of this document is to provide Optigo Seller/Servicers and Third-Party consultants of Moderate Rehabilitation Loans best practices and guidance to ensure successful loan processing. This document is not all-inclusive of all details required.

Moderate Rehabilitation Loans require ongoing monitoring reports that detail progress of the renovations, identify any deficiencies with the workmanship or materials, and track adherence to the renovation schedule and budget. Upon completion of the renovations, these loans also require lien waivers and certifications from several parties to verify that the project was completed as intended, is of good quality, and is legally compliant.

### Servicer Qualifications

- Servicers must be aware of the financing nature of the monthly servicing required, and the critical differences between this and the servicing of a routine repair escrow.
- Servicer must have in-house personnel with experience servicing construction/renovation loans who are able to service the Disbursement Agreement and Disbursement Servicing Agreement, or a reputable third-party servicer experienced with construction/renovation loan servicing that can be hired to assist Seller/Servicer with its responsibilities under the Disbursement Agreement and Disbursement Servicing Agreement.
- At the time of underwriting, Renovation Servicing Team's Qualifications must be submitted to Freddie Mac in the form of resumes and summary of experience with similar projects. Members of the servicing team to include individuals responsible for administration and those responsible for physical inspections. It is encouraged that the Architectural Consultant who provided the Pre-Construction Analysis Report conduct the physical inspections for the ongoing renovations. See *Moderate Rehabilitation Best Practices: Property Condition Due Diligence* for further details.
- ❖ **BEST PRACTICE:** Before the Mod Rehab loan has rate-locked, the Seller/Servicer must provide its qualifications/experience to Freddie Mac for approval, and confirm either acceptance or requirement to hire a qualified third party, in order to avoid false expectations and last-minute negotiations on this critical issue.
- ❖ **BEST PRACTICE:** Once the Mod Rehab loan has closed, a servicing kick-off call should be conducted between Seller, Primary Servicer, and Freddie Mac to establish contacts and expectations during the renovation period. This call can also occur during underwriting.

### Renovation Draws

- Renovation draws/disbursements will adhere to the Disbursement Servicing Agreement between Freddie Mac and Seller/Servicer, and the Disbursement Agreement between Seller/Servicers and Borrower.
- Draw requests are typically submitted monthly, for a minimum amount of \$100,000.

### Servicer Responsibilities

- Servicer to review all change orders, to ensure revisions do not impact the scope or quality of renovations and to ensure sufficient funds remain to complete the project.
- Servicer to coordinate draw inspections with the Third-Party Inspector in advance to prevent undue delays in draw processing. These inspections should occur when the contractor's payment request for the current period is ready in draft form. The Third-Party Inspector should meet with a representative of the contractor on site to inspect the property and review the payment request to ensure the work represented by the payment request is complete as requested.
- Servicer to coordinate periodic calls with Freddie Mac to discuss progress of renovations in greater detail than is provided in the status summaries in the monthly Disbursement Certifications.

- Borrower to Seller/Servicer – Disbursement Agreement:
  - Borrower submits to Seller/Servicer a Disbursement Request, which includes the AIA Forms G702 and G703 (these forms must include a lien waiver from the general contractor).
  - Borrower will receive disbursement from Seller/Servicer within 10 business days of satisfactory delivery of Disbursement Request
  
- Seller/Servicer to Freddie Mac – Disbursement Servicing Agreement:
  - Seller/Servicer submits to Freddie Mac a Disbursement Certification (the form which is attached as an exhibit to the Disbursement Servicing Agreement), which identifies the draw amount, the trailing 3-months NRI and occupancy, and a brief summary of renovation status.
  - Within 5 business days after submitting the Disbursement Certification, Servicer is required to deliver to Freddie Mac the backup material associated with the requested disbursement (a “disbursement package”) including:
    - Payment request AIA Forms G702 and G703 (received from Borrower)
    - Third-party inspector’s report (in compliance with the *Freddie Mac Multifamily Guide* (Guide), Chapter 63.4)
    - Title insurance policy date-down endorsement or other state-specific construction financing endorsement
    - Confirmation of required NRI performance with rent roll
  - If property fails to meet the performance metric (breakeven NRI) set forth in the Disbursement Agreement, Freddie Mac is not obligated to fund the requested disbursement.
  
- Retainage:
  - Five percent (5%) of each advance shall be retained by Freddie Mac. Upon certification of Substantial Completion by the Architect of Record or the General Contractor, the 5% retainage will be released subject to the holdback defined in the Disbursement Agreement.
    - In the event there is no Architect of Record or General Contractor, a borrower’s certification to that effect will suffice.
  - The final holdback will be released upon satisfaction of all requirements as detailed in the *Final Disbursements Requirement* section of the Disbursement Agreement.
  
- Servicer Requirements Before Final Disbursement:
  - Satisfaction of all requirements as detailed in the *Final Disbursements Requirement* section of the Disbursement Agreement including (not limited to):
    - Borrower’s Certification, confirming all renovations have been fully paid for, and no claims exist that may result in a lien against the property.
    - Non-consolidation Opinion, if the loan amount is greater than or equal to \$25,000,000.
    - Post-Construction Analysis Report – this is a hybrid report that contains elements of both a Property Condition Assessment and Construction Documentation Close-out Review. Reference Sections 62.3-62.7 and 63.5(a)-(c) of the Guide for additional information.
  
- ❖ **BEST PRACTICE:** The Post-Construction Analysis Report (PCAR) should review the Property Condition Report (PCA) and Pre-Construction Analysis Reports created at origination. The PCAR should also build their analysis from the Monitoring Reports that were prepared throughout the renovation process.

### Third-Party Inspector

- Third-party inspectors providing construction monitoring reports must meet the qualifications set forth in the Guide, Chapter 63.2(a), and the inspector’s reports must meet the standards set forth in the Guide, Chapter 63.4.
- Inspectors are responsible for preparing the monthly Renovation Monitoring Reports submitted in connection with each draw request. These reports must include the following:

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- Review of contractor's executed payment application, change orders, updated project schedule, test results, and inspection reports by local building authorities and (if applicable) the architect of record.
  - The inspector's findings of project renovation (Is the project progressing according to schedule? Is it on budget? Percent complete?)
  - An opinion on the impact of Change Orders (executed and proposed)
  - An opinion of the quality of workmanship and materials.
  - Adequacy of remaining hard cost funds and contingency.
  - Factors that may delay completion, and any applicable solutions.
- The final inspection will prepare for the Post-Construction Analysis report which must:
- Confirm that the project was completed substantially in accordance with the construction documentation submitted at underwriting
  - Confirm that the quality and workmanship is acceptable
  - Confirm that the project meets all applicable governmental requirements
  - Confirm that the pre-construction reserve analysis is still valid
  - Confirm that the property has no Priority Repairs (including PR-90 repairs)
  - Review all construction completion documentation
- ❖ **BEST PRACTICE:** Recommended that the same Architectural Consultant who prepares the Pre-Construction Analysis Report also prepare the on-going Renovation Monitoring Reports so they are familiar with the scope of the project and the property. See *Moderate Rehabilitation Best Practices: Property Condition Due Diligence* for further details.

**Four months prior to the conversion date**, an abbreviated underwriting package will be required. As part of this package updated third-party reports, including but not limited to an Appraisal and a Post-Construction Analysis Report will be required. Notwithstanding the foregoing, a full underwriting package is required if Additional Loan Proceeds are being requested.

- ❖ **BEST PRACTICE:** Six months prior to conversion date, reach out to your Freddie Mac representative for further details regarding the abbreviated underwriting package or Additional Loan Proceeds. See *Moderate Rehab Best Practices: Conversion* for more information.