



# Bulletin

**NUMBER: M2017-8**

**TO:** Freddie Mac Multifamily Sellers and Servicers

December 14, 2017

## **SUBJECTS**

With this Bulletin for the Multifamily Seller/Service Guide (Guide), Freddie Mac is:

- Including underwriting improvements intended to streamline the underwriting process
- Revising the requirements for third party reports for certain non-SBL Mortgages when the initial amount of the Mortgage is \$15 million or less, or the Mortgage is a Supplemental Mortgage and the combined initial principal balance of the Supplemental Mortgage and the unpaid principal balances of any senior Mortgages encumbering the Property are \$20 million or less in the aggregate
- Eliminating the requirement that a Borrower that is a limited liability company with a single member be formed in Delaware, when the initial amount of the Mortgage is \$15 million or less
- Revising our requirements for Properties with aluminum wiring
- Adding requirements for preferred equity
- Updating our insurance requirements
- Updating our requirements for Green Up<sup>®</sup> and Green Up Plus<sup>®</sup>
- Making minor changes to our requirements for a guarantor that is an investment fund
- Updating our requirements for the consultant that performs a property inspection to provide information for a construction report
- For SBL Mortgages, updating the requirements for property financial statements to be submitted in the underwriting package
- Updating our provisions for submission of the rent roll component of the Quarterly Financial
- Revising the timing for when a nonrefundable application fee will be deemed earned by Freddie Mac for certain Mortgages
- Updating the notification method for adverse matters/non-monetary defaults
- Announcing upcoming changes to the annual certification process
- Making miscellaneous housekeeping changes

### Effective dates

All revisions announced by this Bulletin are effective immediately.

### Conclusion

More details on these changes are provided on the pages that follow. Guide text for the changes announced in this Bulletin is highlighted in green on AllRegs, with the exception of the text of Chapter 66, which will be published in black. If you have any questions about this Bulletin, please call your Freddie Mac representative.

Sincerely,

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Multifamily Underwriting and Credit

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## Streamlined Underwriting Requirements

As announced at the recent Customer Conference, we are revising our requirements for O&M Programs, Moisture Management Plans (MMPs) and problematic materials, as follows:

- An asbestos O&M program is required only if friable asbestos-containing materials (ACM) will remain present at the Property after the Origination Date of the Mortgage
- An O&M program for polychlorinated biphenyls (PCBs) is required only if the PCB-containing equipment is not owned by a utility and was manufactured prior to July 2, 1979
- The environmental consultant is permitted to make a professional judgement on whether the Property should have an MMP

We are revising the requirements for asbestos to emphasize the role of the consultant in inspecting the Property for evidence of ACM, identifying the location and condition of any suspect materials and collecting samples of materials suspected of containing friable ACM. If certain conditions exist, the consultant may recommend that the friable ACM remain in place; under these circumstances, the consultant must recommend an O&M program. The Borrower must institute an O&M program developed by an environmental professional acceptable to Freddie Mac. These changes can be found in Sections 61.6(a)-(f).

As part of the environmental protocol for PCBs, we are removing the requirement for the environmental consultant to determine the PCB content of any equipment that was manufactured after July 2, 1979. For utility-owned equipment for which the PCB content is unknown or confirmed to be in excess of 50 PPM, the environmental consultant is no longer required to recommend an O&M program to manage the equipment in place. These changes can be found in Sections 61.11(a)-(d).

In Sections 8.3(a), 61.14(c) and (d), we are revising our requirements to permit the environmental consultant (or physical risk consultant, if applicable) to make a professional judgement about whether an MMP is required to address potential ongoing water and Mold issues. If an MMP is recommended, the Borrower must establish the program prior to the Origination Date.

## Third party reports for Certain Non-SBL Mortgages

We are changing our requirements for third party reports for a non-SBL Mortgage with the following characteristics:

- The Mortgage has an initial principal balance of \$15 million or less, or the Mortgage is a Supplemental Mortgage and the combined initial principal balance of the Supplemental Mortgage and the unpaid principal balances of any senior Mortgages encumbering the Property are \$20 million or less in the aggregate
- The Mortgage is not a Moderate Rehabilitation Mortgage, a Lease-up Mortgage, a Value-add Mortgage, or a Forward Commitment Mortgage

The changes for Mortgages meeting the above conditions are as follows:

- Seller/Service providers have the option to provide Freddie Mac with new Form 1108, Physical Risk Report, in lieu of an environmental report and a property condition report
- A zoning report is not required if the appraiser provides a zoning analysis in the Appraisal; however, certificates of occupancy are still required

- A wood-damaging inspection report or a certification from the current pest control provider is not required if the Borrower provides documentation that there is a wood-damaging insect contract in place for the Property

To accommodate these changes, we have

- Created Form 1108, Physical Risk Report, which will be available on FreddieMac.com and AllRegs<sup>®</sup> by December 22
- Added Chapter 66, Physical Risk Report Requirements, to provide instructions on completing Form 1108
- Revised Sections 5.3(a), 8.2(e), 8.5, 41.4(c), 60.12(g) and various entries in Section 55.2 that provide requirements for building code violation documentation, the Physical Risk Report, wood-damaging insect documentation, and zoning documentation
- Updated the cash underwriting checklist found in Exhibit 1, Section 1.1
- Made minor changes, but no substantive revisions, to Chapters 62 and 62SBL for consistency with Chapter 66

#### Borrower that is a Limited Liability Company (LLC)

We have revised Section 9.2(e) to state that a Borrower that is a limited liability company with a single member will not be required to be formed in Delaware for a Mortgage with the following characteristics:

- The Mortgage has an initial principal balance of \$15 million or less
- The Mortgage is not a Moderate Rehabilitation Mortgage or a Forward Commitment Mortgage

#### Aluminum Wiring

We are revising our requirements for Properties with aluminum wiring to require that the property condition or physical risk consultant must identify all branch wiring terminations that are unsafe, not code-compliant, or are not a “permanent repair” as indicated by the Consumer Product Safety Commission, and must identify any previous repairs to the connections. We’ve updated Section 62.5(c) to reflect these changes.

For Properties with aluminum wiring, we’ve also updated Section 8.2(d) to require the Seller to submit a cost estimate and certification of completion for any repairs or corrections required due to unsafe conditions or as required by any applicable code.

#### Preferred Equity

We are including the following information in the Guide with respect to preferred equity:

- The characteristics of the type of equity contributions that require Freddie Mac consent
- Requirements for an acceptable Preferred Equity Investor
- Requirements for the Redemption Date
- The amount of a Preferred Equity Contribution
- Unacceptable attributes of a Preferred Equity Contribution
- Requirements for a guaranty of a Preferred Equity Contribution
- A requirement that the Governing Agreement contain a prohibition against modifying any of the terms of the Preferred Equity Contributions

- A Requirement for the Seller/Service's legal counsel to complete the Preferred Equity Analysis form
- Additional underwriting information required by Freddie Mac.

These changes can be found in Sections 11.6(a)-(i).

### Insurance Updates

We are revising Section 31.2(b) to state that Freddie Mac will permit an insurance policy of any term, if the policy is in full force and effect on the Origination Date of the Mortgage and coverage will remain continuous through the term of the Mortgage. We no longer require the Seller/Service to provide Freddie Mac with evidence that the policy is eligible for renewal if the policy will expire within 90 days of submission of the full underwriting package.

### Green Up and Green Up Plus Mortgages

Freddie Mac is making the following updates to its requirements:

- The Borrower must commit to complete sufficient energy or water improvements to result in a projected minimum energy or water consumption savings of 25 percent, based on whole building consumption
- We are removing the requirement that the budget for Green Improvements must average \$350 per unit
- We are no longer suggesting that a Property is likely to benefit from an energy and water audit if the Property was built prior to 2000 or is at least 15 years old (for a tax credit loan)

These changes can be found in Sections 24.3(a) and 65.1(a).

### Investment Funds

With respect to an investment fund, we are adding a requirement that the Seller/Service must provide any information requested by Freddie Mac when Freddie Mac reviews an application for a Mortgage with an investment fund guarantor.

This change can be found in Section 9.10(a).

### Consultants Permitted to Conduct Property Inspections

We are revising our requirements to permit either a property condition consultant or an Architectural Consultant to conduct a property inspection that provides content for a construction report. We still require the construction report itself to be prepared by an Architectural Consultant meeting the requirements of Section 63.2(a).

This change can be found in Section 63.1(a), 63.1(b) and 63.3(a).

## Property Financial Statements for SBL Mortgages

We are revising our requirements for the property financial statements that an SBL Seller/Servicer must include in an underwriting package.

For the historical property financial statements, the Seller/Servicer must submit, if available, a certified operating statement that includes the prior three full years. However, if a Year 3 statement is not available, the Seller/Servicer must submit:

- Year 1 back statement, and
- Year 2 back statement, if available

For current property financial statements, Freddie Mac strongly prefers the Seller/Servicer to submit a T-12 operating statement; however, if this statement is not available, a year-to-date financial statement is acceptable.

With respect to monthly collections:

- Freddie Mac strongly prefers a T-12 statement
- A T-3 certified financial statement, including collected monthly net residential income (NRI) for at least the prior three months provided
- In the absence of financial statements with net residential income, the Seller/Servicer must provide a Form 1144, Verification of Collections.

These changes can be found in Section 55SBL.2 under the entry for property financial statements.

## Submission of the Rent Roll Component of the Quarterly Financial

We are revising Section 40.4(c) to indicate that a rent roll will now be considered current if it is dated no more than two months prior to the original due date. For example, if the Quarterly Financial due date is August 31, the rent roll is considered current if dated on or after June 30. This change aligns with the recent updates made to the Freddie Mac Property Reporting System.

## Nonrefundable Application Fee

We are revising the timing for when a nonrefundable application fee will be deemed earned by Freddie Mac for Conventional Cash Mortgages, TAH Cash Mortgages, TAH Cash Forward Commitment Mortgages, Supplemental Mortgages and Seniors Housing Mortgages. The application fee will now be deemed earned by Freddie Mac at the earlier of delivery of the full underwriting package or 30 days after the date the Borrower executes the Seller Application. The change can be found in Sections 17.11(e), 19.8(e), 19A.8(e), 20.6 and 21.9. We have also added a definition for the Seller Application to the Glossary.

## Notification of Adverse Matters/Non-Monetary Defaults

We are revising Section 44.6(a) to require Servicers to notify us via email instead of by telephone.

## Upcoming Changes to the Annual Certification Process

Freddie Mac relies on the annual certification reports to provide a snapshot of the status of our Seller/Servicers and Servicers, and their ability to continue doing business with Freddie Mac. For Seller/Servicers and Servicers with a fiscal year ending on December 31, 2017, the following forms will be due to Freddie Mac on March 31, 2018.

- Form 16M, Multifamily Annual Certification Report
- Form 17M, Multifamily Annual Certification Report – Structured Transaction & Tax-Exempt Bond Seller/Servicers
- Form 1110M, Multifamily Annual Certification Report – Servicer Only

We will be making revisions this year to Forms 16M, 17M and 1110M. Freddie Mac will officially release the updated Forms 16M, 17M and 1110M system in the Multifamily Eligibility System in early 2018 and will announce the changes to these forms in an upcoming Guide Bulletin.

## Miscellaneous Housekeeping Changes

We are updating the following Forms as we have applied minor, non-substantive changes to the Forms to correct a misspelling, to expand the width of certain fields and update references to renumbered Guide Chapters:

- Form 1115, Borrower and Borrower Principal Certificate and
- Form 1115-SBL, SBL Borrower and Borrower Principal Certificate
- Form 1104, SBL Physical Risk Report
- Form 1105, Property Condition Assessment