

# Bulletin

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NUMBER: 2010-20

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TO: Freddie Mac Sellers and Servicers

August 31, 2010

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**SUBJECT: MORTGAGES SECURED BY PROPERTIES WITH AN OUTSTANDING PROPERTY ASSESSED CLEAN ENERGY (PACE) OBLIGATION**

This *Single-Family Seller/Servicer Guide* (“Guide”) Bulletin provides guidance to our Seller/Servicers regarding Freddie Mac’s purchase of Mortgages secured by properties with a Property Assessed Clean Energy (PACE) or PACE-like obligation.

**BACKGROUND**

In our Industry Letter dated May 5, 2010, *First Lien Mortgages and Energy Efficient Loans*, Freddie Mac reminded Seller/Servicers that an energy-related lien may not be senior to any Mortgage delivered to Freddie Mac. We also indicated that we would provide additional guidance regarding our requirements on energy retrofit lending programs in the future, should they move beyond the experimental stage.

On July 6, 2010, the Federal Housing Finance Agency (FHFA) issued a Statement on Certain Energy Retrofit Loan programs, such as PACE programs (“the FHFA Statement”). The FHFA Statement advised that First Liens offered by most PACE programs “pose unusual and difficult risk management challenges for lenders, servicers and mortgage securities investors,” and change customary lending priorities.

The FHFA Statement further provides that First Liens created by PACE programs raise safety and soundness concerns. Other regulators share these concerns. For example, a Bulletin issued July 6, 2010 by the Office of the Comptroller of the Currency (OCC 2010-25) states, “This lien infringement raises significant safety and soundness concerns that mortgage lenders and investors must consider.”

Freddie Mac supports the goal of encouraging responsible financing of energy efficient and renewable energy home improvements, and we believe this goal may be achieved without altering the lien priority status of first Mortgages or other underwriting requirements. To the extent necessary to mitigate greater risks associated with PACE and PACE-like programs, Freddie Mac will take additional actions. These actions could include adjusting loan-to-value and debt-to-income ratios for Mortgages secured by properties located in jurisdictions that permit such programs.

**REQUIREMENTS**

The requirements of this Bulletin apply to PACE obligations that provide for First Lien priority.

**Mortgages secured by properties subject to PACE obligations that provide for First Lien priority**

Freddie Mac will not purchase Mortgages secured by properties subject to PACE obligations that provide for First Lien priority. Seller/Servicers are responsible for monitoring State and local laws to determine whether a jurisdiction has a PACE program that provides for First Lien priority.

**Mortgages secured by properties subject to PACE obligations originated before July 6, 2010 that provide for First Lien priority**

For Mortgages with Freddie Mac Settlement Dates before **July 6, 2010** that are secured by properties subject to PACE obligations originated before **July 6, 2010** that provide for First Lien priority, Freddie Mac will waive the Uniform Security Instrument requirement that these obligations be subordinate to the First Lien. Otherwise, our requirements regarding Mortgages secured by properties subject to PACE obligations that provide for First Lien priority remain unchanged.

**Refinance of Mortgages secured by properties subject to PACE obligations originated before July 6, 2010 that provide for First Lien priority**

To mitigate the risk posed by PACE obligations that provide for First Lien priority over the Mortgage, we are implementing additional requirements with respect to the refinance of Mortgages with Freddie Mac Settlement Dates before July 6, 2010 that are secured by properties subject to PACE obligations originated before July 6, 2010 that provide for First Lien priority.

For such Mortgages (except when refinanced under Freddie Mac's Relief Refinance Mortgages<sup>SM</sup> offering as described below), Freddie Mac will require that Borrowers who have sufficient equity pay off the existing PACE obligation in full as a condition to obtaining a new Mortgage. In addition, Sellers must qualify the Borrower using the steps below that are designed to mitigate Freddie Mac's exposure and minimize Borrower hardship:

- Sellers must first attempt to refinance the Mortgage either as:
  - A cash-out refinance Mortgage under the requirements of Guide Section 24.6, *Requirements for Cash-Out Refinance Mortgages*, or
  - A "no cash-out" refinance Mortgage under the requirements of Guide Section 24.5, *Requirements for "no cash-out" refinance Mortgages*, except that pay-off of the PACE obligation will be permitted in the same manner that secondary financing that is used in its entirety to purchase the subject property may be paid off

Proceeds from the cash-out refinance Mortgage or the "no cash-out" refinance Mortgage must be used to pay off the PACE obligation in full.

- If the Mortgage does not meet the requirements for a cash-out refinance Mortgage or a "no cash-out" refinance Mortgage, as described above, with sufficient proceeds to pay off the PACE obligation in full, the Seller may then underwrite the Mortgage under Freddie Mac's Relief Refinance Mortgage<sup>SM</sup> – Open Access offering under the requirements of Guide Chapter B24, *Freddie Mac Relief Refinance Mortgages<sup>SM</sup> – Open Access*, with the PACE obligation remaining in place. In underwriting under such offering, it will not be necessary to include the PACE obligation in the calculation of the total loan-to-value ratio; however, the PACE obligation must be included in the monthly debt payment-to-income ratio.

*Special delivery requirements*

For Relief Refinance Mortgages - Open Access when the PACE obligation remains in place, in addition to complying with the special delivery requirements provided in Chapter B24, the Seller must deliver special characteristics code "H28."

## **GUIDE REVISIONS**

Applicable Guide sections will be updated in a future Bulletin to reflect these changes.

## **CONCLUSION**

If you have any questions, please contact your Freddie Mac representative or call (800) FREDDIE.

Sincerely,

A handwritten signature in black ink, appearing to read "Patricia J. McClung". The signature is fluid and cursive, with a long horizontal stroke extending to the right.

Patricia J. McClung  
Vice President  
Offerings Management