Federal Housing Finance Agency

Duty to Serve

FHFA presents Snapshots from Freddie Mac's & Fannie Mae's Duty to Serve Underserved Markets Plans for Small Multifamily & Single-Family Rentals

Effective December 14, 2018

Excerpts from Freddie Mac's and Fannie Mae's Duty to Serve Underserved Markets Plans: Small Multifamily and Single-Family Rentals

Compiled by the Federal Housing Finance Agency

FHFA has compiled excerpts from Fannie Mae's and Freddie Mac's Duty to Serve Underserved Markets Plans addressing activities that support small multifamily and single-family rentals. To access the Duty to Serve Underserved Markets Plans in their entirety, please visit FHFA's Duty to Serve website.

Table of Contents

DISCLAIMER

Implementation of the activities and objectives in Fannie Mae's and Freddie Mac's Duty to Serve Underserved Markets Plans may be subject to change based on factors including FHFA review for compliance with the Charter Acts, specific FHFA approval requirements and safety and soundness standards, and market or economic conditions, as applicable.

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FHFA's Compilation of Snapshots from Freddie Mac's Duty to Serve Plan: Small Multifamily & Single-Family Rentals

Activity 4 –Small Multifamily Rental Properties in Rural Areas: Regulatory Activity

Small multifamily rental properties are an important segment of the rural rental market. A sizable portion, particularly those most affordable, are encumbered by USDA debt and at risk of being lost to the market over time as USDA 515 loans mature and properties can exit the program. This is known as the maturing mortgage crisis.

Freddie Mac intends to focus its small rural properties support in the first Plan Term on addressing the maturing mortgage crisis and leveraging USDA programs by:

1. Developing a new offering to preserve properties with USDA section 515 debt
2. Purchasing loans to preserve properties with USDA section 515 debt
3. Researching and developing a new offering to support USDA's 538 program.

OBJECTIVE A: DEVELOP A NEW OFFERING TO PRESERVE PROPERTIES WITH USDA SECTION 515 DEBT

Evaluation Area	Year	Incomes Targeted	Extra Credit
Loan Product	**1 and 2**	**VLI, LI**	**Not applicable**

USDA's Section 515 program is vital for the preservation of highly affordable rural multifamily housing. It provides rental assistance to ensure that tenants pay no more than 30 percent of their income toward rent. According to an analysis by the Housing Assistance Council (HAC), the USDA has financed approximately 28,000 multifamily properties with over 533,000 units through the Section 515 program.[69] As of early 2016, there were approximately 13,830 properties with 416,000 units still in the program. HAC has determined that the following number of units will exit the 515 program by 2040 based on their loan maturity dates:[70]

Years	2017-2027	2028-2032	2033-2040
Annual Unit Loss	1,800 units	16,000 units	22,600 units
Cumulative Units Lost Per Period	18,000 units	64,000 units	158,200 units
Cumulative Units Lost	**18,000 units**	**82,000 units**	**240,200 units**

Per our analysis of the 515 portfolio on data.gov, we estimate that 75 percent of these units are in rural areas. And among rural 515 properties, 94 percent have between five and 50 units.

When these units exit the program, affordable housing is lost in rural areas because owners will no longer be able to access the rental assistance that enables them to preserve rents at affordable levels to residents making very low incomes for their area while maintaining the property. This is often referred to as the “maturing mortgage crisis.” We have repeatedly heard from advocacy groups that USDA’s annual budget is not sufficient to preserve this number of properties at the rate at which they would exit the program. Therefore, the introduction of private capital is necessary to recapitalize and preserve these properties to maintain this important housing stock for rural communities.

In response, Freddie Mac has developed a strategy that would address the maturing mortgage crisis by increasing product flexibility and partnering with the USDA to create a sustainable, effective loan product offering. Initially, Freddie Mac will perform a comprehensive review of our current product offerings to determine how we can best leverage our existing products with the market challenges faced by the rural rental housing market. Additionally, we will collaborate with borrowers and our seller/servicers to help design additional features that can be added to support this loan offering. Based on the results of our review and feedback from our collaboration, we intend to make improvements consistent with prudent underwriting standards to ensure safety and soundness. We also intend to leverage our market-leading risk-distribution methods that allow us to attract private capital to support these properties, offer competitive terms and flexibility to our borrowers, and transfer risk away from taxpayers. This capability is fundamental to providing persistent liquidity and stability to the market.

While somewhat premature, we expect that these enhancements will cumulatively have a significant impact on the borrowers of rural rental housing by providing a source of stable, efficient, long term private capital which will enable very low-, low-, and moderate-income tenants to remain in their homes without additional rent burden. We expect that, if successful, these improvements will result in increased purchase volume and additional liquidity to this market. Over the two-year period, Freddie Mac plans to build a strong offering foundation by publishing an initial term sheet and completing a pilot transaction to determine market acceptance and long term feasibility of the product offering. We also plan on providing training to our seller/servicers to ensure that they are equipped with the information needed to accurately promote and support the offering.

Baseline

While we have originated Tax-Exempt Loan transactions, we lack the legal infrastructure, agreements with USDA, and stakeholder partnerships to leverage this execution for a successful loan offering for portfolios with USDA 515 debt. We last purchased a loan on a Section 515 property in 2010, so our baseline of recent experience is zero transactions. This is to be expected because the vast majority of transactions involving USDA’s Section 515 properties use other USDA programs, such as Section 538 or the preservation and rehabilitation (MPR) program.

Challenges, Actions and Market Impacts

Market Challenge	Freddie Mac Action
Limited financing sources ▪ Apart from USDA's Section 538 Guaranteed Rural Rental Housing Program, there are very few outside debt sources being used in conjunction with USDA's Section 515 program. This is due to the tightly integrated USDA requirements between USDA programs. **Property features** ▪ 515 properties, given their small size, cannot benefit from the same economies of scale as more typical multifamily urban or suburban properties due to the number of units. Across the 515 portfolio, the average property size in rural markets is 29 units, per our analysis of 515 properties from data.gov. ▪ Smaller rural properties are also distant from major employers and access to other resources that provide occupancy stability to a rental property. **Number of stakeholders** ▪ Through our research, we have learned that each transaction has multiple stakeholders, each with its own requirements that impact the loan parameters and some of which are conflicting, making it difficult to ensure ease of execution for each transaction. **Reliance on USDA 515 debt** ▪ USDA 515 debt ensures that the property maintains rental assistance. Therefore, it is important that any additional financing be compatible with USDA 515 debt. **Reliance on rental assistance** ▪ Many USDA 515 properties rely on the rental assistance provided by the Section 521 program. Without this rental assistance, very low- and low-income renters would be overburdened and unable to fulfill rent obligations. The USDA 521 program provides borrowers with a one-year contract to cover rent payments on behalf of tenants in a designated number or percentage of the units. The one-year contract is only renewed as many times as	**Year 1 – 2018** 1) Evaluate the barriers limiting private capital in conjunction with USDA's Section 515 program to identify product parameters and legal document requirements. 2) Engage with the following participants to assess and identify areas of opportunity for our product: three issuers from states with a high concentration of 515 properties, two borrowers from the Council for Affordable and Rural Housings top 20 borrowers list, two rural advocacy organizations, and two Freddie Mac Seller/Servicers. 3) Evaluate and assess alternative loan structures to determine offering parameters, as evidenced by the following term sheet. 4) Evaluate and assess appropriate underwriting parameters to mitigate risk of rental assistance termination. These underwriting parameters will be captured in our internal credit policy and summarized in the product term sheet. Results of this analysis will be included in our term sheet. 5) Publish an official product sheet on our website that defines the product and its purpose to enable borrowers and sellers to understand the new loan product. The term sheet will contain at least the following elements: a. Product overview and loan purpose b. Sponsor and property eligibility requirement c. Loan-to-Value Limits d. Debt coverage Limits e. Allowable lengths of loan term f. Allowable lengths of amortization 6) Initiate one sample transaction to test market acceptance of the new loan and legal structure introduced to the market. Given the time it takes to complete a transaction, we will not likely make a loan purchase until Year 2. 7) Provide one to three training sessions via webinar or in person for Freddie Mac sellers

funds are made available. **Product awareness** ▪ Borrowers are accustomed to working specifically with USDA lenders to originate rural rental housing loans. Likely, the Freddie Mac loan product will have a different loan and legal structure than the current financing option to this market. ▪ Freddie Mac sellers may not be motivated to market and originate this business due to its initial small scale, limited inventory, and amount of time it takes to originate a loan. From our current outreach, we have heard that it can take from two to five years to complete a rural rental housing transaction.	to provide loan offering details, benefits to the borrower, and origination procedures to ensure that sellers have the knowledge to market the product effectively. To address the sellers' concerns, information will be provided to the sellers regarding incentives and origination efficiencies to motivate them to originate transactions with USDA 515 debt. 8) Negotiate and implement subordination agreement with USDA to ensure USDA 515 debt will stay on the property with the senior Freddie Mac debt. The finalized agreement will be shared with FHFA on an informational basis. **Year 2 – 2019** 1) Provide two additional training sessions as needed to ensure Freddie Mac sellers are well informed about the Freddie Mac loan offering and can accurately articulate its benefits to their borrowers. 2) Complete a pilot transaction and initiate two additional pilot transactions for purchase in 2020. The pilot will be deemed successful if either we purchase the loan, or we receive sufficient information to inform a report of lessons learned. 3) Draft a summary report of lessons learned based on the pilot transaction for use in product refinements. The summary will be shared with FHFA on an informational basis. 4) Update the product sheet and terms based on feedback from stakeholders and the summary report.
Resource Challenge	**Freddie Mac Action**
▪ Multiple resources from various teams within Freddie Mac will be essential to ensure success of the actions outlined above.	**Year 1 – 2018** 1) Implement an internal working group to ensure that all resources are allocated appropriately and alignment is maintained throughout the creation of the new loan product. **Year 2 - 2019** 1) Debrief with Freddie Mac, the borrower, and the seller on the sample transaction to determine positive and negative aspects of the origination process and product structure.

Market Impacts

While the challenges are many, the benefit to the market is great, both in the near term, as we lay a strong product foundation and refine it through a pilot transaction, and in the long term, as we, along with the USDA, are able to provide long-term liquidity and stabilize the 515 preservation market while preserving the rental assistance (subject to continued federal support for these programs). By designing this offering to leverage our market-leading risk-distribution methods, we will be able to attract private capital to support five-to-50-unit 515 properties in rural markets and the tenants who live in them. In so doing, we will transfer risk away from taxpayers and promote safety and soundness.

Ultimately, though, the benefit of this offering is clear: Through this work, we will enable tenants of very-low and even extremely-low income, many of whom are senior citizens, to be able to continue to live in safe and decent housing that is affordable to them in their communities. Not only does this benefit the tenants themselves, but it also promotes stable communities across rural America.

OBJECTIVE B: MAKE PURCHASES TO PRESERVE PROPERTIES WITH USDA SECTION 515 DEBT

Evaluation Area	Year	Incomes Targeted	Extra Credit
Loan Purchase	**3**	**VLI, LI**	**Not applicable**

Purchases of loans on properties with USDA 515 debt are an integral part of our strategy of providing liquidity in support of five-to-50-unit properties in rural areas. Indeed, per analysis of the 515 portfolio on data.gov, 93 percent of the 515 properties in rural areas are between five and 50 units.

After establishing and piloting a loan product for properties with 4 percent tax credits and USDA 515 debt, Freddie Mac will focus on the purchase of loans on these properties. This will provide relief from the maturing mortgage crises and preserve affordability for rural properties. Maintaining long term affordability is key to providing rural areas with a stable source of housing. As a result of our outreach, we have determined that properties with USDA 515 debt are usually originated in portfolios of multiple properties and it could take as long as three years to originate one portfolio with USDA 515 debt.

Given the many challenges of providing financing for 515 properties, purchasing loans and promoting those purchases and their replicability through press releases or deal stories will be fundamental to growing this market over time.

Baseline

We have not made any purchases of loans on properties with Section 515 debt in several years; therefore, we do not have a representative baseline.

Target

In Year 3 (2020), we plan to purchase two portfolios of loans on properties with USDA 515 debt that include properties with five to 50 units in rural areas. This target is dependent upon us initiating these transactions in Year 2 (2019). If our loan product requires adjustments, we will likely adjust this target based on market feedback on our product offering.

Challenges

There are several challenges involved in purchasing loans on properties with USDA Section 515 debt. These challenges are present both externally in market conditions and internally through necessary underwriting and infrastructure changes.

First, there are the limited financing sources for these properties. Apart from USDA's Section 538 Guaranteed Rural Rental Housing Program, there are very few outside debt sources being used in conjunction with USDA's Section 515 program. This is due to the tightly integrated USDA requirements between USDA programs. Borrowers are accustomed to working specifically with USDA lenders to originate rural rental housing loans. Likely, the Freddie Mac loan product will have a different loan and legal structure than the current financing option to this market.

Second, many USDA 515 properties rely on the rental assistance provided by the Section 521 program. Without this rental assistance, very-low and low-income renters would be overburdened and unable to fulfill rent obligations. The USDA 521 program is different from long-term HAP contracts, which Freddie Mac has a history of doing. The USDA 521 program provides borrowers with a one-year contract to cover rent payments on behalf of tenants in a designated number or percentage of the units. The one-year contract is only renewed as many times as funds are made available. Because the Section 521 rental assistance is only available if 515 debt is still on the property, it is important that any additional financing be compatible with USDA 515 debt.

Third, unlike most markets, where one could expect awareness and transactions to be initiated and closed in the same year, this is far less likely to be the case for properties with USDA 515 debt. These transactions are highly complex with multiple parties, multiple properties, and sometimes challenging market conditions. Even once initiated, a transaction can fall through due to many factors, such as disruptions in the LIHTC equity market, rising interest rates, or change in local market conditions.

Market Impacts

The immediate benefit of these transactions will be to rehabilitate and preserve safe, decent, and affordable rental homes for tenants who are at risk of becoming homeless if these properties exit the 515 program. This cannot be understated in the near term or in the long term. Indeed, these initial loan purchases lay the foundation for more third-party financing and enable long-term, stable liquidity, which is fundamental to providing long-term residence to thousands and thousands of people and families.

These transactions will also be precedent setting. Through these transactions we will demonstrate to rural developers that there is a new and replicable source of innovative financing for 515 properties that will enable the recapitalization and rehabilitation of these properties. Upon completion, we will issue press releases and/or publish news stories on our website that summarize the transactions and promote their replicability, which will lay a foundation for growth in purchases in future years.

In so doing, we will introduce new standards and efficiencies into the market. We will also look to attract private capital and promote safety and soundness by leveraging our capital markets infrastructure and risk-distribution capabilities.

We recognize that these innovations will likely take some time to catch on, as each transaction in the early years will likely be slow to develop, and new opportunities will likewise be slow to follow. However, with each transaction, we will preserve more affordable rental homes and build more momentum and market adoption so that by the time 515 properties start to mature at scale around 2028, the market has a well-functioning and well-tested execution in place to preserve a meaningful share of rental homes for tenants in need.

OBJECTIVE C: RESEARCH AND DEVELOP A NEW OFFERING TO SUPPORT THE USDA SECTION 538 ROGRAM

Evaluation Area	Year	Incomes Targeted	Extra Credit
Loan Product	**2 and 3**	**VLI, LI, MI**	**Not applicable**

Freddie Mac recognizes that there is a large need to serve small properties in rural areas, which are often associated with USDA subsidies. Outside of the 515 program, the 538 program is the next most prevalent single source of financing for small, five-to-50-unit rural properties. This program has grown in scope and budget in recent years, and has been well adopted. Based on our preliminary discussions with rural mortgage lenders and borrowers, there is some market interest in Freddie Mac purchasing 538 guaranteed loans, whether or not these loans also support 515 properties.

The 538 program has unique parameters that may or may not be compatible with Freddie Mac's infrastructure and risk-distribution network. Moreover, there are nuances to the use of this program that need to be better understood before we can develop a product that will provide additive benefit to the market.

In Year 2 of our Plan, we intend to conduct a research effort to better understand the market for small rural multifamily properties, the role of the 538 program in supporting them, the geographic distribution of 538 loans relative to the need for financing, and the 538 program parameters that might influence where and how this program is used. While we intend to use this research to aid in our product development efforts, we believe it is important to make this research public as well to increase awareness of the financing needs and opportunities in rural markets and attract more private capital to support rural properties and communities. Therefore, we will publish a report on our findings in 2019.

Based on our research completed and published in Year 2, we plan to act upon our findings and develop a loan offering in Year 3 to support properties with USDA 538 debt. At this time, it is difficult to determine the scope and parameters of the new offering without a better understanding of the market, but the following guiding principles will apply:

1. We will seek to provide additive benefit that extends the reach or scope of the 538 program.
2. We will maintain prudent credit standards to ensure long-term stability and safety and soundness.
3. We will seek to attract private capital to rural markets by leveraging our market-leading risk-distribution methods, such as our K-Deal and PC executions.

By staying true to these principles, we anticipate that our offering will provide the market with greater access to capital to preserve long term affordability of small multifamily properties in rural areas, and enable the further growth of the 538 program.

Baseline

To date, we have had preliminary conversations with rural mortgage lenders and the USDA to understand the 538 program and determine that there is potential for Freddie Mac to have a role supporting this program. We have not performed or published formal research on the 538 program, nor do we have experience purchasing 538 guaranteed loans.

Challenges, Actions and Market Impacts

Supporting small rural properties through the 538 program poses several challenges, from the disparate geographic locations, to borrower awareness, to challenging local economies that may affect the long-term occupancy of small properties. These challenges, as well as the actions we will take to address them, are summarized below:

Market Challenge	Freddie Mac Action
Limited scope and awareness of the 538 program ▪ The 538 program serves an important segment of rural markets, and is well known within the rural financing market. However, it is not so well known in the broader market due to its specialized nature and the closely tied network of lenders and Ginnie Mae investors. This lack of awareness will make it challenging to identify Freddie Mac investors who have an interest in supporting the 538 program. **Product awareness** ▪ Borrowers are accustomed to working specifically with a few lenders to originate 538 loans, only two of which are also Freddie Mac Multifamily seller/servicers. **Lender acceptance** ▪ The level of effort to finance a small property is just as much as to finance a large property, but typical lender compensation structures do not reward them equally for their efforts. This compensation structure creates a disincentive to pursue financing for small properties. Freddie Mac sellers may not be motivated to market and originate this business due to its initial small scale and limited inventory. **Borrower and property features** ▪ The borrower set for this offering may be different than the traditional Freddie Mac borrower. ▪ Rural rental properties cannot benefit from the same economies of scale as urban or suburban properties due to the number of units. Per our analysis of 2015 American Communities Survey data, 83 percent of rural multifamily properties have fewer than 50 units.	**Year 2 – 2019** Build broader market awareness of the 538 program by publishing research in a report on our website. 1) Report will evaluate the scope and potential of the 538 program based on data from the following sources: National Housing Preservation Database, data.gov, HUD, and Census Bureau. 2) In support of our report, we will take the following actions: a. Engage with at least two experienced 538 lenders to understand their use of the program and their needs for Freddie Mac as a secondary market participant. b. Engage with at least one leading researcher on rural markets and the 538 program to help inform and structure our research. 3) Report will include the following: a. Market size estimate for current and potential small properties that could be candidates for 538 debt b. Geographic distribution of current 538 properties and the geographic scope of the program c. Assessment of opportunities for Freddie Mac to maximize the impact of the 538 program 4) Publication of research on our website will be accompanied by a press release **Year 3 – 2020** Develop and release loan offering to support the 538 program. Product development and roll out will include the following: 1) Implement internal working group to ensure all resources are allocated appropriately and alignment is maintained throughout the

	product development process. 2) Develop and/or update Freddie Mac legal documents to support the section 538 guarantee. 3) Establish credit parameters as evidenced by a product term sheet. 4) Publish official product term sheet on our website that defines the product and its purpose to enable borrowers and sellers to understand the new loan product. The term sheet will contain at least the following elements: a. Product overview and loan purpose b. Sponsor and/or property eligibility requirement c. Loan-to-Value Limits d. Debt coverage Limits e. Allowable lengths of loan term f. Allowable lengths of amortization 5) Provide one to three training sessions via webinar or in person for Freddie Mac sellers to provide loan offering details, benefits to the borrower, and origination procedures to ensure that Sellers have the knowledge to market the product effectively. To address the seller's concerns information will be provided regarding incentives and origination efficiencies to motivate sellers to originate transactions with USDA 538 debt. 6) Initiate one pilot transaction to test market acceptance—depending on when the product is released and this transaction is initiated, we may not purchase the loan during this Plan Term.

Market Impact

USDA's 538 program has provided meaningful benefits to the rural market, particularly for five-to-fifty unit properties, and has increased in scope since its inception. At present, the primary market for 538 loans is limited to four lenders, and the only secondary market for 538 loans is through Ginnie Mae. This limits the overall reach of the program and its ability to help more rural renters. By developing a broader market understanding of the 538 program and the benefits it provides, and by developing a Freddie Mac execution to support the 538 program, we will extend both the primary market for these loans, as we release the offering to our Targeted Affordable seller/servicer network and add lenders to the 538 market, and the secondary market through Freddie Mac. Through our risk distribution methods, we will be able to attract more private capital to rural markets. Over time, as demand for 538 loans increases, there is potential for the allowable federal authorization for the 538 program to increase, which would further help to attract more private capital to support rural markets and provide safe and decent affordable housing to tenants across rural America.

Activity 5 – Single-Family Rental in Rural Markets: Additional Activity

Based on our research of the rural market, 66 percent of rural renters live in single-family rental (SFR) homes: 49 percent in one unit homes, and 17 percent in two-to-four-unit homes. This important segment of the rural rental market is not specifically defined in the Duty to Serve regulation. However, it is a significant source of housing for rural renters. The market for SFRs lacks standardization, and this lack of standardization leads to variances in tenant opportunities and the quality of SFRs in which they reside.

Under current financing models, SFR renters are generally not served by the GSEs. We believe it is our mission to serve all renters in all areas of the market, and we are well situated to provide financing for this market due to our expertise in managing credit risk and strict property and borrower requirements. Our involvement in the SFR market will lead to greater standardization and more decent affordable housing for its tenants. Our intent is to provide liquidity, stability, and affordability to properties that provide quality affordable housing to the rural rental market. Therefore, in order to more fully support the rural market and provide the benefits of GSE financing to the majority of rural renters, Freddie Mac is including single-family rentals in rural markets as an additional activity.

While the size of the single-family rental market has increased in the years after the economic downturn of the past decade, it has consistently been a large portion of the market. Pre-recession data, from 1985-2005, show that single-family rentals have consistently made up 10-12 million units, or 30-35 percent, of the renter market share. Since 2005, this sector has been the fastest growing segment of rental occupied households, adding an additional four million single-family rental units or up 35 percent in the 10 years ending 2015, per Freddie Mac's tabulations of the American Community Survey.[71]

As the SFR market continues to mature, several distinct stratifications of market participants have emerged. The most sophisticated of these participants are large institutional investors that have entered the SFR business and have established a new institutional asset class that does not replicate the apartment industry or flip houses. However, the institutional participants make up only a small percentage of the total SFR market. Based on discussions with market participants, including lenders and borrowers, and other research, we believe it is appropriate to tier SFR owners as follows:

- Institutional participants:
  - Typically own portfolios of 1,000 or more single-family rentals
  - Estimated total population of 25 investors
  - Estimated to hold approximately 200,000 properties
  - Estimated value of market share of SFR is $30 billion (1 to 2 percent of total market)
- Middle-tier participants:
  - Typically own portfolios of 11 to 1,000 single-family rentals
  - Estimated total population of 77,000 investors
  - Estimated to hold approximately 1.8 million SFR properties
  - Estimated value of market share is $300 billion (10 percent of total market)

- Smaller participants:
    - Typically own portfolios of one to 10 single-family rentals
    - Estimated total population of approximately eight million investors
    - Estimated to hold approximately 13 million SFR properties
    - Estimated value of market share is $2.5 trillion (85 to 90 percent of total market)

With respect to SFRs generally, we see the opportunity to provide standardization and liquidity to the market, and promote better quality standards and affordable housing opportunities for residents, particularly with sponsors who have between 50 and 2,000 properties and five years or more experience. We intend to do this in such a way that we can promote affordability relative to the broader market in which homes are located, as well as improve available rental options. While rural SFRs will be part of a diversified and national SFR business model, in order for a transaction to receive Duty to Serve credit, we will require that (1) a certain share of the units (described below) in a SFR transaction will be located in rural markets and affordable at 100 percent of AMI or below.

Our product development and lending activities will provide longer-term financing than is typically available, which will reduce costs to borrowers and promote greater stability via less-frequent refinancing. We will also place a high priority on establishing industry-leading standards and best practices and imposing those standards on our borrowers, sellers/servicers, and applicable properties. Those standards will be designed to ensure the preservation of the quality of the housing and the neighborhoods in which they are located and underscore our commitment to the highest standard of care in the promotion of safe, decent, high-quality housing. We will focus on property age and condition, borrower experience with SFR, borrower financial stability and covenants, capital reserves and other transaction specific features to ensure long-term stability and quality.

Additionally, Freddie Mac will make commitments to neighborhood stability by seeking to maintain the residential character of the homes and seeking to support, not disrupt, existing communities. If Freddie Mac were to become a key liquidity provider in the SFR market segment, more owners would strive to meet the standards we established. Just as “agency quality” has come to mean decent, well-managed conventional multifamily housing, we would lift the quality of SFR as well.

In years 1 through 3 of our Plan, we intend to explore how to serve rural areas through this activity, through outreach and product development, culminating in loan purchases.

The benefit to tenants is clear: better quality housing, more stable rents, and more affordable rental options across rural America.

OBJECTIVE A: RESEARCH RURAL SFR MARKET CHARACTERISTICS AND OPPORTUNITIES

Evaluation Area	Year	Incomes Targeted	Extra Credit
Outreach	**1**	**VLI, LI, MI**	**Not applicable**

While there is emerging research on the overall SFR market, there is much less work done on SFRs in rural areas. This lack of research makes it harder for us, or other financing providers, to support this market and attract private capital. Therefore, in Year 1 of our Plan, we intend to perform market research and outreach to better understand the nature of, and opportunity for, SFRs in rural areas, including high-needs rural regions. We will publish a report of our market analysis in 2018. Given that we are likely to do market research on the entire SFR market, the report on rural may be a subset of a broader market study. We will also leverage this research and report in our product development efforts.

Baseline

While Freddie Mac has performed research on the SFR market for the purposes of this Plan and for discussion with FHFA, this research has not had a focus on rural markets, the opportunities and challenges presented there, and the particular ways in which we can best support these markets. This study will likely be the first of its kind published for public use, and will provide an important foundation for product development and lending activites.

Challenges, Actions and Market Impacts

Market Challenge	Freddie Mac Action
▪ Market is in a stage of fragmentation and emerging standardization ▪ Large variations in financing, operating performance, and servicing standards ▪ Difficulty in developing new offerings to support this market ▪ The rural SFR market is not well understood, and there is no major capital distribution framework servicing it today ▪ Data sources on SFRs are limited. Throughout the course of our research there have been instances where data was temporarily unavailable or where combining sources proved to be more difficult than originally anticipated. Our SFR research will rely heavily on data, and completing the objective within a narrow timeframe will be very difficult if data issues are encountered. **Resource Challenge** ▪ Throughout the Duty to Serve Plan, we are taking on a considerable number of research efforts, all of which require extensive planning, as well as collaboration with key stakeholders, and analysis.	**Year 1 – 2018** 1) Identify and aggregate data on the SFR and rural markets from the Census Bureau and other sources we identify in our research. 2) Engage with at least three operators, three property managers, and three lenders to better understand their interest and activity in rural markets as well as credit standards they apply or operate under. 3) Engage with at least one leading researcher on rural markets or SFRs to better inform our approach and analysis. 4) Publish report on SFR market including a rural focus. The report will likely include the following, though these factors may change as we engage in our research: a. Analysis of market size and opportunities b. Analysis of property types c. Analysis of geographic concentrations d. Analysis of existing credit standards used by lenders in the market today

The design and research of all of these objectives will have many unique components, and will leverage the expertise and skills of our internal research organization, whose focus extends beyond the scope of the Duty to Serve Plan.	5) Publish the report on our website and promote it with a press release.

Market Impact
In rural areas, multifamily properties are not necessarily the preferred rental option, as populations tend to be deconcentrated, and the housing stock leans heavily towards single-family homes. SFRs are an important source of rental housing, but the market is still in a stage of fragmentation and emerging standardization. In the mid-tier market across the country, there are approximately 77,000 different investors who have portfolios of more than 10 SFRS, for a total of 1.8 million properties. In rural markets, that is considerably smaller, though the share is not yet known. The lack of foundational understanding of this market, and the lack of clear financing options for these properties makes it difficult for investors and renters alike to sustain this market. By performing and publishing our foundational research, we will provide clarity of understanding necessary to attract private capital at scale, lend to support SFRs, and distribute risk away from taxpayers. This research will also be fundamental to our product development efforts, especially for rural areas, and will enable us to better set standards for this market that will benefit tenants over time.

OBJECTIVE B: DEVELOP OFFERING FOR SFR TRANSACTIONS CONTAINING HOMES IN RURAL AREAS

Evaluation Area	Year	Incomes Targeted	Extra Credit
Loan Product	**1 and 2**	**VLI, LI, MI**	**Not applicable**

In Year 1 of our Plan we intend to develop offering terms for SFR transactions that include, but are not limited to, homes in rural areas, and in Year 2 we will look to execute a sample transaction that includes rural homes. In order to support rural SFRs in a safe and sound manner, it will be important to avoid concentration risk. Therefore, we will look for transactions to have geographic diversity, including beyond rural areas, which will also enable stronger standardization across this asset class, and consequently, enable better terms for rural borrowers and choices and conditions for rural renters. In order for an SFR transaction to receive Duty to Serve credit, however, we will set a minimum concentration of rural units in that transaction. To determine that threshold, we looked at the overall concentration of SFRs in rural markets, then adjusted based on several factors with a goal of being able to support more transactions, and therefore more rural properties over time.

From our tabulations of 2015 American Community Survey data, we understand that 21 percent of all one-to-four-unit SFRs are located in rural markets. Not all of these are likely to be financeable by Freddie Mac, however, for various reasons, such as the quality of individual homes, size and experience of the sponsor, and proximity to other homes. We suspect that many of these are owned by borrowers who do not have a sufficient portfolio size or experience to meet our lending criteria. Also, we suspect that there are very few borrowers or lenders who have a sizable concentration of rural-only or majority-rural portfolios.

Given this, we believe for Duty to Serve credit, it is appropriate to require that the lesser of 50 units or 10 percent of the units in a transaction be located in a Duty to Serve-designated rural area and be affordable at 100 percent of AMI or below as a starting point in our product development efforts. If, in our product development and market research efforts, we find that these parameters need to be adjusted, either upward or downward, in order to better support the rural market, we will update them as necessary.

In developing this offering, we will work with lenders experienced in SFRs, as well as with sponsors who have 50 to 2,000 units of SFRs under management and at least a five-year history of operations. This history of operations is important in assessing the quality of the borrower and their experience both operating a sound business and servicing tenants. In cases where we are working with banks and smaller institutions, our offering will have substantial benefit, as we will enable these institutions to recycle capital for more lending. Today these institutions tend to hold their loans on their balance sheets, which limits new loan production and restricts liquidity. As a secondary participant, Freddie Mac can purchase these loans and create needed liquidity. With our involvement, these institutions will be able to make more loans and support more people and communities.

In Year 2 of our Plan, we will seek to engage in at least one SFR transaction with sufficient units in rural areas. This transaction will allow us to test and refine the offering parameters we develop in 2018, as well as provide valuable information to us and the market about these transactions.

Also in Year 2, with the goal of improving market standardization and sharing best practices, Freddie Mac will collect, analyze and disseminate data relative to the SFR business model for all markets, including a rural market breakout. For the SFR sector, this includes collecting, compiling, and publishing data and research to allow for a better understanding of the sector and its risks in order to facilitate increased investment. We anticipate collecting and evaluating information related to operating expenses, capital expenditures and appropriate replacement reserve levels, occupancy rates by market compared to standard multifamily, rental per square foot, best practices regarding insurance, asset inspections and legal documentation and financing structures. To the extent possible, we will also capture available data related to the impacts of SFR activities on homeownership within various market segments, including homeownership rates, preserving affordability and neighborhood stabilization. Ultimately, Freddie Mac will establish quantitative and qualitative criteria for the deals that we will support and promote those criteria to encourage investors to use them. These criteria will yield high-quality loans with Freddie Mac's investment-quality standards.

By performing this research at the same time as our sample transaction, we will have the ability to contemporaneously learn from analytical work and transaction experience.

Baseline

Freddie Mac does not currently offer a SFR product today. In 2017, we have been developing relationships within the SFR industry as part of expanding our understanding of the SFR market. To date, staff have attended the largest single-family rental conference and have held meetings with owners/operators, valuation and home inspection vendors, securitization agencies, and other industry groups. As a result, Freddie Mac has been able to inspect SFR homes in markets across the country, learn acquisition and exit strategies, explore valuation options and better understand the investment perspective of Middle-Market owners and the SFR securitization market. These relationships have allowed Freddie Mac to better understand the need for long-term financing priced effectively for sponsors with 50 to 2,000 properties.

Challenges, Actions and Market Impacts

Underwriting Challenge	Freddie Mac Action
▪ The SFR market has a unique set of underwriting requirements that are difficult to line up with multifamily approaches and systems. ▪ The property management capabilities of each	**Year 1 – 2018** Meet with at least three operators, three property managers, and three lenders to determine best practices for underwriting, property management, and financing parameters.

SFR sponsor can vary considerably, and need close attention on a case-by-case basis.	1) Attend at least two SFR conferences for education. 2) Establish underwriting parameters as evidenced by a term sheet for a SFR loan product that will contain at least the following elements: a. SFR collateral type b. Loan term c. DCR and LTV loan sizing criteria d. Amortization e. Minimum loan size f. Property release and substitution requirements g. Minimum number or percentage of units in rural areas to receive Duty to Serve credit 3) Establish legal infrastructure to support these transactions in a safe and sound manner.
Market Challenge	**Freddie Mac Action**
▪ There are many factors that place constraints on the market for SFRs: ▪ Current market lenders do not support properties with an appraised value of $50,000 or less. ▪ Current lenders do not have a viable and scalable secondary market. ▪ Limited understanding of the size and scope of SFRs in rural areas. ▪ There is not a cost-effective inspection and evaluation process given disparate locations. ▪ Appraisals can be challenging in areas where there are limited comparable properties. ▪ There is not a cost-effective legal, title, and insurance review process, given the disparate locations of properties and number of properties included in transactions. ▪ There is currently not an industry standard for risk distribution or connection to the capital markets except in select cases with large institutional investors.	**Year 1 – 2018** 1) Publish a term sheet on our website for a SFR loan product that will contain at least the following elements: a. SFR collateral type b. Loan term c. DCR and LTV loan-sizing criteria d. Amortization e. Minimum loan size 2) Directly engage with at least three lenders to promote this product. 3) This pilot will be available nationally, and will be required to include a portion of the units in rural markets, as described above. **Year 2 – 2019** 1) Attempt at least one sample transaction under this product with a qualifying sponsor that includes homes in rural markets, as described above. 2) Collect and analyze data on overall SFR and rural SFR market performance to allow for a better understanding of the sector and its risks in order to facilitate increased investment. Data collected will include the following: a. Operating expenses

	b. Capital expenditures and appropriate replacement reserve levels c. Occupancy rates by market compared to standard multifamily properties d. Rental per square foot e. Best practices regarding insurance f. Asset inspections and legal documentation g. Financing structures 3) Draft and publish a report of analysis of data collected above and lessons learned from our sample transaction and how that transaction fits in the context of the data collected. 4) This report will provide a better understanding to the market of standards that could be applied to provide more liquidity and benefit tenants. 5) Report will be published on our website and promoted with a press release. 6) We will view this pilot as successful if we either purchase at least one loan under the offering or receive sufficient market feedback to produce the report described above.
Resource Challenge	**Freddie Mac Action**
▪ SFRs require a dedicated team of producers and underwriters, risk distribution, and servicing professionals with expertise in this market.	**Year 1 – 2018** 1) Assemble a team of production, underwriting, capital markets, and servicing professionals with expertise in the SFR market to ensure that our offering and operations are well considered and can be well executed. 2) Provide one to three training sessions covering product process and parameters, including underwriting and servicing responsibilities to internal staff via webinar or in person training sessions as appropriate for the audience. 3) Provide one to three training sessions covering product process and parameters, including underwriting and servicing responsibilities to seller/servicers via webinar or in person training sessions as appropriate for the audience.

Market Impact
Single-family rental housing is a large fragmented market in need of standardization. To ensure safe, decent, and affordable housing choices for renters across the country, and particularly in rural areas, this market needs liquidity and strong credit standards, the combined effect of which will lead to greater choice for renters and

safer, better housing options.

Establishing a new loan product, legal infrastructure, and risk distribution framework will take a great deal of internal effort and deep commitment. To develop this offering, the following must occur: establish underwriting requirements in an unfamiliar market; establish legal, inspection, servicing, and risk distribution standards; create a specialized production, underwriting, and legal team; create a product term sheet, and continue outreach to SFR market participants. This product will be built from the ground up and will be a first of its kind.

Our research and report in Year 2, including our pilot transaction, will be fundamental to market development as well because this information will set standards for how SFRs can be most effectively financed and will better inform our product development efforts. This report will also provide fundamental information to capital markets investors, allowing them to better understand this market. Their improved understanding will enable us to better channel their capital to rural SFRs.

The combination of these efforts will establish an entirely new secondary market for SFRs in rural areas and beyond, providing substantial benefit to renters and communities alike, and promoting necessary underwriting and quality standards across the industry, which will broaden renter choices among safe, decent, and affordable housing options. This product will also allow us to leverage private capital to provide long-term liquidity and stability, while distributing risk away from the taxpayer.

OBJECTIVE C: PURCHASE SINGLE FAMILY RENTAL LOAN(S) SUPPORTING RURAL AREAS

Evaluation Area	Year	Incomes Targeted	Extra Credit
Loan Purchase	**3**	**VLI, LI, MI**	**Not applicable**

In Year 3 of the Plan, we intend to build on our product development efforts and deliberately measure our SFR purchases, with a target of at least five SFR transactions that contain homes in rural markets. Our strategy will be to work with banks who have both a demonstrated history of financing SFR and have a substantial portfolio of SFR properties on their balance sheets and/or, through our seller/servicers network, with borrowers who have financed between 50 and 2,000 properties and have a history of sound operations.

Baseline

This product will be our first involvement in this market, therefore our SFR in rural markets baseline is 0 transactions.

Target

In Year 3, our preliminary target is to complete five SFR transactions with the lesser of 50 rural units or at least a 10 percent share of the units in the whole transaction as rural and be affordable at 100 percent of AMI. If, in our product development and market research efforts, we find that these parameters need to be adjusted, either upward or downward, in order to better support the rural market, we will update these parameters and inform FHFA through a plan modification.

Challenges

The SFR market in rural areas is constrained by several factors. Currently, there is limited debt capital available for longer-term (7 or 10 years) financing needs. Without longer-term capital, properties need to be financed more often, which increases costs to the borrower and puts pressure on rents to cover financing costs. This challenge is exacerbated by the absence of a viable secondary market for SFR loans for sponsors who hold between 50 and 2,000 units. Without a secondary market, banks are not able to lend as much or as freely as they would be required to hold the loans on their balance sheet (which contains their available capital to lend), and tenants do not benefit from the uniform credit standards imposed by Freddie Mac.

There is also uncertainty specifically in the size and scope of the rural SFR market, especially with sponsors who have sufficient portfolio size and experience. In our early stages of engagement in, and standardization of, this market, we expect there will be few transactions until sponsors better understand the offering from Freddie Mac and the benefits we can provide.

Market Impacts

Freddie Mac's commitment to purchase SFR loans with underlying homes in rural areas will start to bring an efficient, assured source of debt capital financing to this segment of the SFR market, and promote standardization and affordability. As noted, there is a need for SFR as an affordable rental option in rural areas due to either limited multifamily supply or SFR as a preferred option for these areas. The varying and costly debt financing options available for these SFR homes today makes it difficult for borrowers and renters alike to provide and find safe and decent affordable housing. By channeling private capital through our innovative risk distribution methods for longer-term loans, we expect over time to promote greater SFR home availability as a desired, safe rental option in rural markets. Without previous experience in the SFR market in rural areas, our involvement in purchasing loans will have a substantial visible impact, and in cases where we are working with banks and smaller institutions, our offering will have additional benefits, as we will enable these institutions to recycle capital for more lending. Today these institutions tend to hold their loans on their balance sheets, which limits new loan production and restricts liquidity. As a secondary market participant, Freddie Mac can purchase these loans and create needed liquidity. With our involvement, these institutions will be able to make more loans and support more people and communities.

These initial transactions, which would be the first of their kind, will be foundational and precedent setting, forming the basis for what we anticipate will be a repeatable program of increasing support for a vital form of rural rental housing. To raise awareness of these transactions and their potential replicability, we will issue a press release or press releases and/or publish one or more news stories on our website highlighting these transactions and their impact.

Fannie Mae

FHFA's Compilation of Snapshots from Fannie Mae's Duty to Serve Plan: Small Multifamily & Single-Family Rentals

D. Regulatory Activity: Small multifamily rental properties in rural areas (12 C.F.R. § 1282.35 (c) (4)).

1. *Objective #1: Identify market opportunities to purchase small multifamily loans in rural areas (Partner and Innovate, Do What We Do Best).*

Meeting the Challenges
Providing liquidity for small loans in rural markets faces a number of challenges, including: • A lack of standardized loan guidelines and documentation among active lenders in rural areas. • Few comparable properties for underwriting purposes. • Challenging economics including population decline, unemployment, and communities that are small and geographically widespread. • Little to no economies of scale for lenders in rural markets. To address these challenges, Fannie Mae will: • Develop and implement a proactive focus on the acquisition of mortgages on small multifamily rental properties in rural areas rather than responding only to lender deliveries. • Strategically identify DUS lenders that have an interest in and focus on rural housing and actively work with these lenders to generate business to increase liquidity to the market. • Purchase small multifamily loans that preserve Section 515 properties financed by the USDA. • Review Fannie Mae's existing small multifamily loan and rural products with a focus on potential product enhancements necessary to increase liquidity for small multifamily loans in rural areas. • Purchase small multifamily loans on MHC located in rural areas and owned by non-profits, government entities, and residents.

SMART Factors
Fannie Mae will undertake the following measurable Actions in the years indicated.

Year	Actions
2018	• Conduct outreach to six Fannie Mae DUS lenders that had previously indicated their interest in originating small multifamily loans in rural areas, to determine their level of interest. • In addition to reaching out to DUS lenders interested in making small multifamily loans in rural areas, conduct outreach to at least two other financial entities to determine if they have the capacity and the resources to become a Fannie Mae lender (or aggregator) with a special focus on rural areas (e.g., lenders with a rural focus that are not currently Fannie Mae lenders, Federal Home Loan Banks, and/or similar financial organizations with a rural footprint, and national CDFI with a rural focus). • Conduct and document an internal review of Fannie Mae's RD 538 program to determine if it could be used efficiently to purchase small multifamily loans in rural areas. • In conjunction with the activities under the Affordable Housing Preservation Market section of this Plan, research potential USDA 515 refinance opportunities in rural areas.

Year	Actions
	• Review and determine one to three changes to Fannie Mae's Small Loan guidelines that would be appropriate to facilitate the provision of liquidity to the market through purchases of the subject loans, taking into consideration notions of safety and soundness. • Position one existing Fannie Mae lender to start originating small multifamily rural loans in 2019 of the Plan. • In order to generate increased small multifamily rural loan purchases, educate the lenders that have expressed interest in small multifamily rural loans via Fannie Mae's outreach on any changes that have been made to the small loan product guidelines. • Utilize results from actions taken during 2018 to confirm the 2019 loan purchase goal.
2019	• Based on the work completed in 2018, purchase 60 loans on small multifamily properties in rural areas, representing a 58 percent increase over the Baseline. ○ **Baseline:** The three year average of the number of small multifamily loans in rural areas purchased by Fannie Mae is 34 loans, with 38 loans purchased in the peak production year of 2015 (2014: 26; 2015: 38; 2016: 37). The prior three year loan purchase results do not reflect any specific marketing approach to small multifamily rural loan purchases. Therefore, assuming Fannie Mae makes a focused effort on improving the loan product and increasing loan purchases, small multifamily loan purchases in rural areas would increase significantly. Using the 2015 peak production amount of 38 loans during the last three years as the Baseline then, the 2019 loan purchase goal will be set initially at 60 small multifamily rural loans. • Complete the on-boarding process for new lenders as needed. • Confirm the 2020 small multifamily rural loan purchase goals.
2020	Based on the work completed in 2018 and 2019: • Increase the purchase of loans to 80 loans on small multifamily properties in rural areas, representing an approximate 110 percent increase over the Baseline. • Develop a plan for small multifamily rural loan purchases for the 2021 – 2023 rural Duty to Serve Plan.

With an affirmative approach with specific interested lenders, Fannie Mae believes the market opportunity available in this market will accommodate significant increases in small multifamily loan purchases. Fannie Mae has significant experience working with our lenders and engaging in activities to increase lending in specific markets. Based on this experience and the available resources, Fannie Mae has determined that this Objective is realistic and may be achieved within the time periods described. All product enhancements, approval of new lenders, and loan purchases will be supported by thorough economic, risk, operational, and counterparty analyses, subject to Fannie Mae's governance and approval processes, and only undertaken consistent with safety and soundness concerns.

Criteria	2018	2019	2020
Evaluation Factor:	Loan Product	Loan Purchase	Loan Purchase
Income Levels:	Very Low-, Low-, and Moderate-Income Levels for all Years		

DISCLAIMER

Implementation of the activities and objectives in Fannie Mae's and Freddie Mac's Duty to Serve Underserved Markets Plans may be subject to change based on factors including FHFA review for compliance with the Charter Acts, specific FHFA approval requirements and safety and soundness standards, and market or economic conditions, as applicable.

Updated January 2019