Federal Housing Finance Agency

Duty to Serve

FHFA presents Snapshots from Fannie Mae's & Freddie Mac's Duty to Serve Underserved Markets Plans for Rural Rental Production

Effective January 1, 2018

Snapshots from Fannie Mae's and Freddie Mac's Duty to Serve Underserved Markets Plans: Rural Rental Production

Compiled by the Federal Housing Finance Agency

FHFA has compiled Snapshots from Fannie Mae's and Freddie Mac's Duty to Serve Underserved Markets Plans addressing activities that support rural rental production. To access the Duty to Serve Underserved Markets Plans in their entirety, please visit FHFA's Duty to Serve website.

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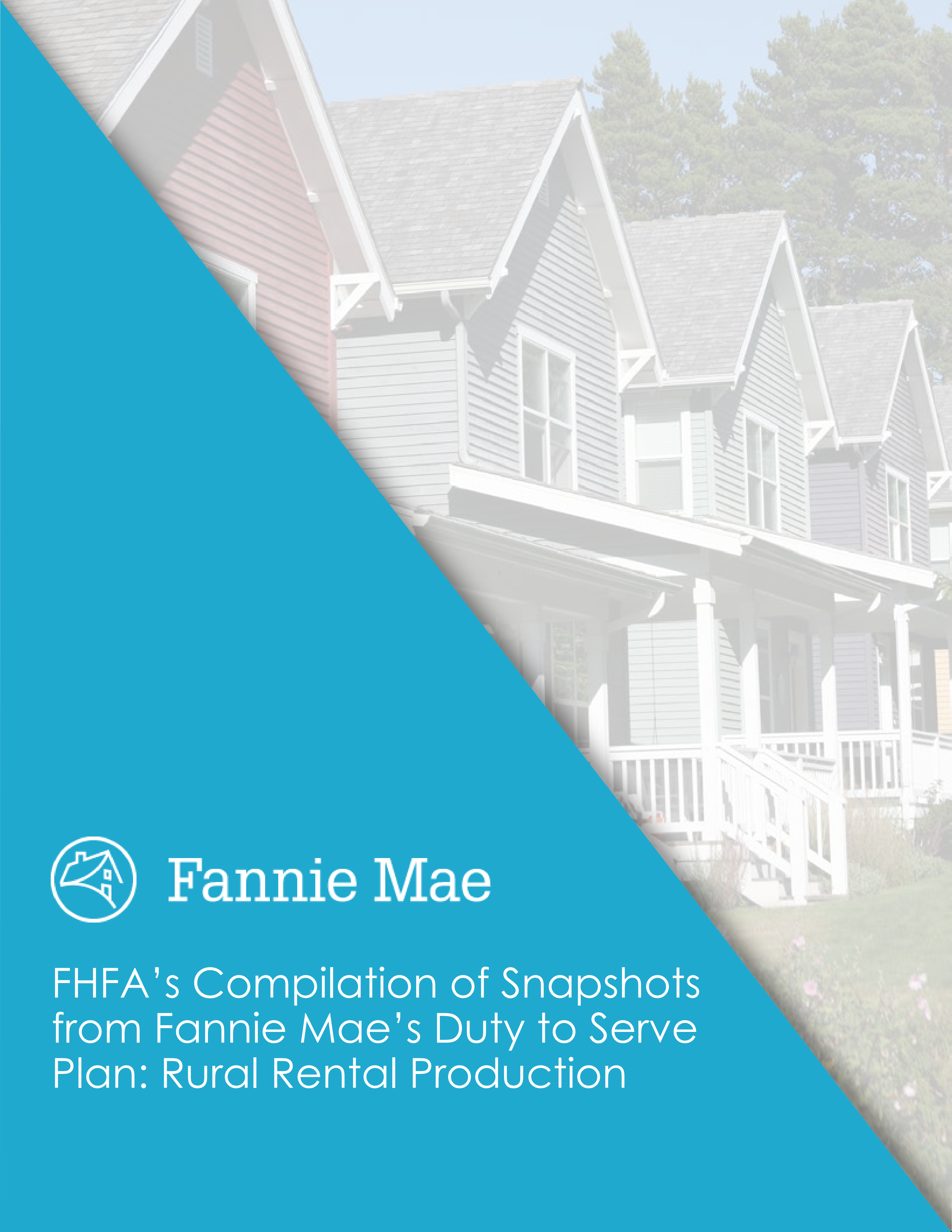

Fannie Mae

FHFA's Compilation of Snapshots from Fannie Mae's Duty to Serve Plan: Rural Rental Production

C. Statutory Activity: The rural rental housing program under Section 515 of the Housing Act of 1949, 42 U.S.C. § 1485.

1. *Objective #1: Work with the USDA and other stakeholders to adopt an approach resulting in increased liquidity for preservation of Section 515 properties and purchase Section 515 loans (Partner and Innovate, Do What We Do Best).*

Meeting the Challenges
Financing and preserving Section 515 properties has several key challenges, including: • According to the USDA, there are over 5,000 properties under the Section 515 program that are becoming eligible for prepayment each year during the next 10 years, with a significant increase in annual prepayment eligibility beginning in 2028. • The program supports housing in rural markets where it is subject to many challenges including: small markets with few, if any, comparable properties; declining populations; and the lack of a dependable source of long-term financing due to limited transaction flow, absence of standardization, and a lack of economies of scale. • The requirement that the USDA must have a first lien on the property to retain the rental assistance – which is especially problematic for a secondary market execution. • Many of these properties may not be able to support sufficient traditional debt, thus LIHTC investments are likely to be required. To address these challenges, Fannie Mae will: • Work with the USDA and other key stakeholders to devise and implement an effective strategy that includes an acceptable solution to maintaining the rental assistance on and providing rehabilitation for Section 515 properties that can be replicated in rural communities across the country and be in place when the number of Section 515 properties at risk of exiting the program increases to 164 properties during the term of the 2021 – 2023 Duty to Serve Plan, and to 271 properties during the 2024 – 2026 Duty to Serve Plan. • Consider coupling debt with LIHTC equity and/or relaunching Fannie Mae's permanent loan option for the construction, acquisition, or rehabilitation of rural multifamily properties through the USDA's RD 538 program. • Purchase loans that preserve Section 515 properties.

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

Year	Actions
2018	• Establish a workable strategy to preserve Section 515 properties across the country by undertaking the following: o Meeting with 10 market stakeholders, including rural housing advocates, Section 515 property owners/developers, State HFA, and the USDA to better understand the specific issues with Section 515 properties (e.g., loss of housing stock) and to discuss possible solutions and formulate the most effective and viable strategy. o Engaging with a total of three DUS and special affordable lenders that have experience with Section 515 properties to get insight to ensure that any proposed strategy is viable for potential lenders. o Reviewing Fannie Mae's financing through the USDA's Section 538 program as part of designing an effective strategy to determine if the product could further enhance Fannie Mae's ability to bring liquidity to the Section 515 preservation effort. • Create a comprehensive Section 515 work-plan that will drive loan purchases and other actions during 2019 and 2020. • As part of Fannie Mae's overall LIHTC equity strategy, conduct a review of the potential use of LIHTC equity investments in conjunction with debt on the USDA Section 515 properties. • Process one Section 515 work-plan (including any potential product enhancements) through internal Fannie Mae product development procedures to secure approvals as required. • Formulate one loan purchase and two other goals for 2019 – 2020, with an aim to provide financing annually for at least 10 percent of the total Section 515 properties that could potentially exit the program during the three year term of the Plan. Based on USDA's multifamily housing property preservation tool,

Year	Actions
	122 Section 515 properties could potentially exit the program during the term of the Plan. Accordingly, the loan purchase goal for 2019 and 2020 is to purchase a total of at least 12 loans secured by Section 515 properties. The Baseline will be updated as needed as Fannie Mae's strategy is established during 2018.
2019	• Purchase at least six loans secured by Section 515 properties at risk of exiting the program. o **Baseline:** While Fannie Mae has refinanced a small number of Section 515 properties in the past, operationally they have not been formally identified and tracked by Fannie Mae and therefore, their numbers cannot be ascertained. Fannie Mae has determined that establishing a Baseline as a percentage of the total number of Section 515 properties with maturing or prepayment eligible loans is an acceptable initial estimate. As noted above, Fannie Mae has set an initial target of at least 10 percent of expiring Section 515 properties during the Plan (a total of 12 loans). However, a Baseline will be reviewed in conjunction with the product development process during 2018 and cannot be determined at this time. • Confirm loan purchase goals for 2020.
2020	• Purchase at least six loans secured by Section 515 properties at risk of exiting the program. • Develop loan purchase goals for the 2021 – 2023 Duty to Serve Plan.

According to the USDA, there are over 5,000 properties under the Section 515 program that have maturing loans or are becoming eligible for prepayment each year during the next 10 years, with a significant increase in annual prepayment eligibility beginning in 2028. Several of Fannie Mae's traditional lender partners have experience in the Section 515 market. In the past, refinancing Section 515 properties has been challenging because of the USDA's requirements around rental assistance coupled with the fact that many of these properties cannot support sufficient debt. However, because the USDA has placed a high priority on preservation of the Section 515 stock, Fannie Mae believes that establishing a workable solution consistent with safety and soundness principles will be difficult, but possible. Based on this information, the experience of our lenders, and the available resources, Fannie Mae has determined that this Objective is realistic and may be achieved within the time periods described.

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

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. o **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		

E. Additional Activity: Invest in LIHTC properties to facilitate the provision of affordable multifamily housing in rural areas (12 C.F.R. § 1282.35 (d)).

1. *Objective #1: Invest in LIHTC properties including housing associated with other Statutory and Regulatory Activities (Partner and Innovate, Do What We Do Best).*

Meeting the Challenges
LIHTC equity investment in rural areas has several key challenges, including: • Rural areas may be overlooked as potential investments because they typically are not included in the CRA footprints for larger financial institutions. • Affordable rural housing often depends heavily on the availability of tax credit investments due to the limited capacity of rural multifamily properties to support debt. • Because rural markets do not attract CRA investors, and those economic investors that do deploy capital to the rural market require much higher yields, the price for rural market tax credits is lower. This results in less equity being made available to the rural market. This fact, combined with the limited capacity of rural multifamily properties to support debt, can result in less investment in preservation being made in rural areas and difficulty in both producing and preserving affordable properties within and from the rural housing stock. To address these challenges, Fannie Mae will: • Re-establish our LIHTC investment capacity, including infrastructure, investment criteria, and policies and procedures. • Include LIHTC equity investments in Fannie Mae's multifamily work-plans for high-needs rural regions and for high-needs rural populations.[16] • Fill gaps in demand for capital as the private investor market presence expands and contracts over time, and support the equalization of pricing for tax credit equity currently and over time among all segments of the market, including rural housing, and other challenging projects that are by their nature routinely capital-constrained. • Work with key LIHTC market participants through the Rural Housing Advisory Council to identify opportunities in rural areas with less investor demand, including high-needs rural regions and high-needs rural populations. • Invest in LIHTC equity that will support the development/preservation of affordable multifamily housing in the high-needs rural regions and for high-needs rural populations, which have historically been areas of lower investor demand. • Invest in LIHTC equity eligible for Duty to Serve credit as an Additional Activity pursuant to 12 CFR § 1282.37(c).

SMART Factors

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

Year	Actions
2018	• Research and analyze market opportunities with respect to potential equity investments in LIHTC housing designed to support affordable rural housing, including the following Statutory or Regulatory Activities:

16 As defined under the Regulations.

Year	Actions
	o Project-based rental assistance housing programs under Section 8 of the U.S. Housing Act of 1937, 42 U.S.C. § 1437f. o The supportive housing program for the elderly under Section 202 of the Housing Act of 1959, 12 U.S.C. § 1701q. o Debt financing of LIHTC under Section 42 of the Internal Revenue Code of 1986, 26 U.S.C. § 42. o The rural rental housing program under Section 515 of the Housing Act of 1949, 42 U.S.C. § 1485. o Small multifamily rental properties financed by entities with assets of $10 billion or less. • Fannie Mae will include both high-needs rural regions and high-needs rural populations in our 2018 research and analysis work related to future potential LIHTC equity investments. • Fannie Mae will: o Conduct extensive research to identify rural areas with low investor demand, including high-needs rural regions and for high-needs rural populations. o Meet with at least two LIHTC syndicators that are active in the high-needs rural regions and with high-needs rural populations to better understand LIHTC equity needs and to identify potential investments in the high-needs rural regions. o In conjunction with Fannie Mae's Single-Family outreach efforts, in Q1, meet with the Rural Housing Advisory Council to gain a deeper understanding of the market challenges and identify areas with low investor demand including in high-needs rural regions and for high-needs rural populations. o Conduct outreach to at least 10 State HFA with rural housing needs, and specifically those serving high-needs rural regions and high-needs rural populations, to better understand how their Qualified Allocation Plans address the needs of underserved rural markets. o Create, establish, and document one set of reasonable investment goals to meet the challenges identified through outreach and research related specifically to rural housing. o Create and adopt one work-plan based upon data obtained through research and analysis, to leverage Fannie Mae's longstanding relationships in the LIHTC industry and commence investing in rural LIHTC properties. ▪ Fannie Mae will reach out to LIHTC stakeholders working in high-needs rural regions and with high-needs rural populations in order to include specific related actions in the work-plan. ▪ In addition, the work-plan will include a review of the initial Baseline estimated for 2019 (five LIHTC equity investments) based on the outreach and research completed, including potential investment opportunities in high-needs rural regions and with high-needs rural populations.
2019	• Fannie Mae will execute the work-plan developed in 2018 and acquire five equity investments in LIHTC projects in the rural areas that are eligible for Duty to Serve credit, as identified through 2018 outreach and research efforts while taking into account safety and soundness considerations. o **Baseline**: Fannie Mae has not made any equity investments in LIHTC properties in the last eight years. In addition, these LIHTC equity investments were made when Fannie Mae had a fully operating business with numerous employees reviewing and managing the investments. Based on this experience, Fannie Mae believes that it is reasonable to estimate that we will make five new LIHTC equity investments in 2019.

Year	Actions
	• In conjunction with Single-Family, Fannie Mae will conduct a meeting with the Rural Housing Advisory Council in Q4 to continue to identify challenges in rural areas with less investor demand, and work together to develop solutions, including the use of LIHTC. • Based on Fannie Mae's experience during 2019, Fannie Mae will review and confirm our 2020 LIHTC equity investment goals.
2020	• Fannie Mae will acquire 10 equity investments in LIHTC projects in the rural areas that are eligible for Duty to Serve credit (including but not limited to high-needs rural regions and for high-needs rural populations), as identified in 2018 – 2019 outreach and research efforts while taking into account safety and soundness considerations. • Fannie Mae will review our experience with rural LIHTC investment during the term of the Plan and identify key lessons learned that will inform the 2021 – 2023 Duty to Serve Plan. • Prepare the 2021 – 2023 Duty to Serve Plan.

While LIHTC equity investments were not identified as a Regulatory Activity, in the final Duty to Serve rule, FHFA indicated in its preamble that it ". . . has determined that, under the final rule, Enterprise equity investments in rural areas will be eligible for Duty to Serve credit, subject to approval of such investments by FHFA as conservator," which has now been received.

This Additional Activity contemplates that the LIHTC investments to be made will be eligible for Duty to Serve credit under 12 CFR § 1282.37(c). This Additional Activity is justified because it contemplates investment in housing which otherwise constitutes a Statutory or Regulatory Activity, and, therefore, is comparable. Moreover, it may be significantly more effective for Fannie Mae to invest in these properties rather than attempt to finance their associated mortgages given the often limited ability of these properties to support debt, or to attract non-LIHTC equity capital seeking a market rate of return. To the extent that this Additional Activity represents investments outside of the referenced Statutory and Regulatory Activities, it nonetheless serves the same targeted very low- and low-income families coupled with the same intent of facilitating the provision of affordable rural housing and, therefore, is comparable to other Statutory and Regulatory Activities. The fact that there is a greater share of families with incomes less than or equal to 60 percent of AMI in rural markets than in urban markets in all recent years, coupled with the fact that these families are very likely to be housing burdened, firmly supports the conclusion that existing and potential tenants will benefit from the creation or continued existence of LIHTC properties.

Fannie Mae believes this Objective can be achieved in the time periods described, based on our lengthy and successful history of investing in LIHTC and our ability and capacity to reenter the LIHTC rural equity market. LIHTC investment in rural areas will be based on market research and safety and soundness principles that also may require that Fannie Mae not undertake this Objective. It is important to note that Fannie Mae intends to include LIHTC equity as a potential tool in our discussions and product enhancement work with numerous Objectives in the Plan, including in high-needs rural regions and for high-needs rural populations; Section 515 preservation, small multifamily rental properties financed by entities with assets of $10 billion or less, and financing of Section 202 properties serve as examples. LIHTC equity can play a very important role in preserving affordable housing in many markets beyond rural ones.

The available market opportunity is best illustrated through an examination of the existing data. For example, while not all Section 515 projects receive LIHTC, using the data for the USDA 515 market as a proxy for market opportunity for rural LIHTC investments provides a reasonable approach to estimating market opportunity. According to the USDA, approximately 15,210 units of Section 515 housing will become eligible for prepayment during the timeframe of this Plan. Many Section 515 properties will need LIHTC in order to be or remain financially sound. Using a modest assumption of $15,000 per unit of needed financing, the total potential market for refinancing/recapitalization could be $228,150,000 over the three-year Plan.

Fannie Mae’s participation as an investor and guarantor in the LIHTC market is an important aspect of our affirmative obligation to facilitate the financing of affordable housing for very low- and low-income families established by the Federal Housing Enterprises Financial Safety and Soundness Act of 1992. Fannie Mae’s presence will enhance the stability of the LIHTC program by serving as a reliable source of capital for affordable housing in diverse economic cycles and markets, including rural and underserved geographies and populations. Fannie Mae, as an equity investor, will not displace private funding but will instead supplement much needed capital, while also seeking to balance the distribution of equity capital across the LIHTC market to include those segments of the market that continue to suffer from the limited liquidity identified in this Objective.

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

Freddie Mac

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FHFA's Compilation of Snapshots from Freddie Mac's Duty to Serve Plan: Rural Rental Production

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

<table>
<tr><th>Market Challenge</th><th>Freddie Mac Action</th></tr>
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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
</td><td>
Year 1 – 2018

Evaluate the barriers limiting private capital in conjunction with USDA's Section 515 program to identify product parameters and legal document requirements.
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.
Evaluate and assess alternative loan structures to determine offering parameters, as evidenced by the following term sheet.
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.
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:
<ol type="a">
Product overview and loan purpose
Sponsor and property eligibility requirement
Loan-to-Value Limits
Debt coverage Limits
Allowable lengths of loan term
Allowable lengths of amortization

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.
Provide one to three training sessions via webinar or in person for Freddie Mac sellers

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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 6 – LIHTC Investment in All Rural Areas: Additional Activity

OBJECTIVE A: ENGAGE IN LIHTC EQUITY INVESTMENT IN ALL RURAL AREAS

Evaluation Area	Year	Incomes Targeted	Extra Credit
Investment	**1, 2 and 3**	**VLI, LI, MI**	**Not applicable**

LIHTCs are the most commonly used subsidy to finance affordable rental housing. While we recognize the need for LIHTC investment in high-needs rural regions and populations, we believe there is an unmet need to be fulfilled across the rural market that is consistent with the intention of the Duty to Serve regulation.

Fundamentally, properties that are not in CRA footprints receive less competition for tax credits, and therefore receive lower tax-credit pricing. Based on current market information from the Community Affordable Housing Equity Corporation (CAHEC), a deal based in Charlotte, North Carolina, would receive up to 95 cents on the dollar; while a deal based in Wetzel County, West Virginia, would only receive approximately 86 cents on the dollar. In a hypothetical transaction with $100 million of debt and a need of $6 million of equity, this difference in tax credit pricing equates to a $540,000 funding gap. In order to fill this gap, it would require additional tax credits, soft debt, or a deferral of developer fee.

Essentially, this lower price per credit makes it harder to create or preserve affordable rural housing and exacerbates housing affordability. Therefore, by focusing some of our investment capital in these areas, Freddie Mac will introduce more competition into the rural marketplace, which will improve LIHTC pricing. The higher the LIHTC pricing, the lower the need for a portion of the rent to pay for debt service; thus, increased LIHTC equity pricing makes properties more affordable.

Freddie Mac intends to make LIHTC equity investments in order to help meet the affordable rental housing needs of low-income families in all rural areas. Investing in LIHTC equity will bring many positive changes to the market including but not limited to the following:

- Stability by making long term and consistent investments regardless of market volatility.
- Liquidity particularly for investments that positively impact low-income renters in rural markets, as well as preservation deals and for any other investment type that may not receive consistent investment interest year after year.
- Affordability for investments that may not be as attractive to the largest investors such as preservation deals, Section 8 deals, and bond deals with high losses-to-LIHTC ratios.

While the high-needs rural regions need special and deliberate attention, affordable housing across all of rural America is hard to develop and preserve. Whether geographic areas are defined as high-needs, there are properties across the country that function specifically as a result of LIHTC equity. We believe it is our mission to support the needs of low- and moderate-income families across rural America. LIHTC equity is a key method of funding this mission.

We recognize in creating this LIHTC Equity Investment offering that the fundamentals described and established here are applicable across all LIHTC Equity Investments, with some specific terms tailored to the needs of these populations It will be important to make LIHTC investments that have sufficient geographic diversity to control for concentration risk, invest at a large enough scale to operate a viable and sustainable business that allows us to continually serve these markets, and do so in a safe and sound manner. We will be mindful to make these investments in markets and cases where there is not sufficient CRA-motivated investment already. Indeed, our role will be to support those parts of the market that are underserved by CRA-motived investment.

Freddie Mac will achieve this through a variety of actions that will allow for safe and sound investment. Building a LIHTC equity investment team will help to formalize the Freddie Mac infrastructure and ensure that each investment is well structured and underwritten. Engaging outside counsel will also allow Freddie Mac to establish a legal infrastructure leveraging the expertise of lawyers that are experienced in drafting partnership agreements.

For making investments, our strategy will be as follows

- Attend at least one conference focused on affordable rental rural housing to learn more about challenges and opportunities specific to this product type.
- Meet with at least two LIHTC developers to better understand their challenges and opportunities in this product type.
- Engage with at least three LIHTC syndicators and sign an investment agreement with at least one syndicator through which Freddie Mac will identify LIHTC investments in rural areas.

Baseline

We have not made any LIHTC investments in the last 10 years, so our baseline of investments is 0.

Target

The following targets are inclusive of transactions that will be completed in high -needs rural regions and for high-needs rural populations as described elsewhere in the Plan.

Year	2018	2019	2020
Total Rural Transactions	6	9	12

Challenges

There are several challenges that will be presented when making LIHTC investments in rural markets.

The primary *market challenges* are seen in a lack of investment and volatility of LIHTC allocation.

In the LIHTC market generally, there have also been significant disruptions in the price of credits.

As 2017 has progressed, we saw more and more examples of large scale LIHTC market disruption, two of which particularly highlight the impact:

1. On March 15, 2017, the California Tax Credit Allocation Committee (TCAC) passed a resolution allowing developers to exchange their 2016 nine percent LIHTC allocation for 2017 LIHTCs. Given delays in finding equity investors, developers found it impossible to close in time to complete construction by the end of 2018 (LIHTC deals must be “placed in service”- meaning 100 percent construction completion and receipt of the certificate of occupancy- by the end of the second year after receiving a LIHTC allocation).

2. In the Midwest, the Ohio Housing Finance Agency (OHFA) had to increase the allocation of LIHTC to deals awarded in 2016 because developers were not getting sufficient equity pricing to allow the deals to be economically feasible. Unfortunately, the additional credits had to come from the 2017 allocation, thus reducing the 2017 pool by approximately 12 percent.

Both examples illustrate how, without increased stability, fewer LIHTC assisted units are likely to be built, ultimately hurting low- income families across the country.

Properties in the rural regions have an additional challenge, as they are frequently not in CRA areas that typically attract multiple bids from financial institutions. Lack of investor interest lowers LIHTC pricing, which makes the credits less effective. Additionally, state Qualified Allocation Plans (QAPs) change annually and rural areas may not be as competitive year in and year out for the limited number of deals that receive a LIHTC allocation.

There is a meaningful difference between a LIHTC deal located in a rural county like Wetzel County, West Virginia, where there is not much CRA-motivated demand for investment and one in Charlotte, North Carolina. Based on current market information from the Community Affordable Housing Equity Corporation (CAHEC), a Raleigh, NC-based LIHTC syndicator with 25 years' experience and covering the Southeast, a deal in Wetzel County is expected to receive approximately 86 cents on the dollar while a deal in Charlotte would receive up to 95 cents on the dollar. In a hypothetical transaction with $10MM of debt and a need for $6MM of equity, this difference in tax credit pricing equates to a $540,000 funding gap, which would require additional tax credits, soft debt, or a deferral of developer fee (with payment from cash flow) to close. This gap financing is often more expensive than LIHTC equity.

There are also several underwriting challenges. Transactions in rural areas often require additional review and analysis. Deals in these areas are frequently in smaller markets, often with marketing and lease-up challenges compared to more urban/suburban properties.

Lastly, resource challenges will hinder our ability to make investments, at least in the early years. The first challenge is our need to develop expertise in these markets. Freddie Mac has not originated new LIHTC investments in close to 10 years. Therefore, we will develop expertise in-house or hire new talent to support this offering. Additionally, we will need to develop partnership agreements at both syndicator and individual deal levels. Freddie Mac has not entered a new partnership with a syndicator in close to 10 years and needs to hire expertise to understand the market for LIHTC investors.

Market Impacts

By initiating investments in the LIHTC market for rural locations, Freddie Mac will provide stability to the equity market specifically for investments that are directly impacted by the lack of investment due to investors' tax reform concerns and lack of CRA credit. This is as true for LIHTC properties in rural areas as it is for those in the even harder to serve high-needs rural regions and populations due to the volatility in allocation and lack of investors.

Building a LIHTC equity investment team will help to formalize the Freddie Mac infrastructure and ensure that each investment is well structured and underwritten. Engaging outside counsel also allows us to create a legal infrastructure leveraging the expertise of a lawyer that is experienced in drafting partnership agreements.

Our initial investments will not only provide a meaningful benefit to the people living in rural markets by providing them with safe, decent and affordable housing that is so hard to come by—we will also introduce competition into a segment of the market that lacks it, and often lacks investor interest at all. By doing so, we could potentially increase the price per credit, which could make the development of properties viable where they were not previously, or allow developers to create or preserve more units than they would otherwise.

These investments will also set an important precedent as we build out our market presence and lay the foundation for future investment by us and others.

Activity 4 – USDA Section 515: Statutory Activity

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. [103] 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:[104]

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**

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 enabled 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.

Freddie Mac intends to address this in these ways:

1. Developing a new offering to preserve properties with USDA Section 515 debt
2. Make loan purchases to preserve properties with USDA Section 515 debt

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 and LI**	**Not applicable**

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 Multifamily seller/servicers to ensure that they are equipped with the information needed to accurately promote and support the offering.

Baseline

While we have originated TEL transactions, we lack the legal infrastructure, agreements with USDA, and stakeholder partnerships to provide a USDA 515 preservation debt offering immediately. 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 clear majority of transactions involving USDA's Section 515 properties use other USDA programs, such as Section 538 or the Multifamily Housing Preservation and Revitalization Demonstration Program (MPR). [105]

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 their own requirements that impact the loan parameters some of which are	**Year 1 – 2018** Evaluate the barriers limiting private capital in conjunction with USDA's Section 515 program to identify product parameters and legal document requirements. 1) Engage with the following participants to assess and identify areas of opportunity for our product. These participants include: 3 issuers from states with a high concentration of 515 properties, two borrowers from council for affordable and rural housings top 20 borrowers list, two rural advocacy organizations, and two Freddie Mac seller/servicers. 2) Evaluate and assess alternative loan structures to determine offering parameters, as evidenced by the following term sheet. 3) 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. 4) Publish official product term sheet on our

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 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.

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

5) Initiate one sample transaction to test market acceptance on 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.

6) 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 sellers' concerns, information will be provided to the sellers regarding incentives and origination efficiencies to motivate them to originate transactions with USDA 515 debt.

7) 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

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.

1) Complete pilot transaction and initiate two additional pilot transactions for purchase in 2020. Pilot will be deemed successful if either we purchase the loan, or we receive sufficient information to inform a report of lessons learned.

2) Draft a summary report of lessons learned based on the pilot transaction for use in product refinements. Summary will be shared with FHFA on an informational basis.

	3) Update the product sheet and terms based on feedback from stakeholders and the summary report.
Resource Challenges	**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 seller on the pilot transaction to determine positive and negative aspects of the origination process and product structure.

Market Impacts

While there are many challenges to developing a product to preserve properties with USDA Section 515 debt, the benefit to the market is great. In the near term, we will lay a strong product foundation and refine it through a pilot transaction. In the long term, we, along with the USDA, will be able 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 515 properties and the tenants who live in them. In so doing, we will transfer risk away from taxpayers and promote safety and soundness.

The benefit of this offering is clear: through this work, we will enable tenants of very low and even extremely low incomes[106], 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 the country.

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

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

Purchases of properties with USDA 515 debt are an integral part of our strategy of providing liquidity in support of the 515 program and the rural multifamily housing market. After establishing and piloting a loan product for properties with four 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 that it could take as long as three years to originate one portfolio with USDA 515 debt. While approximately 75 percent of USDA 515 properties fall within rural defined areas, there are a substantial amount of properties with 515 debt that exist across the country. To mitigate the risks involved with the maturing mortgage crisis, we will also support financing of properties outside of rural areas.

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

Baseline

We have not made any purchases of loans on properties with section 515 debt since 2010, therefore our three-year average baseline is 0.

Target

Prior to the creation of this third-party financing offering, there is no precedent to accurately determine the market for this product. Also, these transactions are highly complex and slow to develop. Therefore, in Year 3 (2020), we plan to purchase two portfolios of loans on properties with USDA 515 debt. This target is dependent upon us initiating these transactions in Year 2 (2019), as these transactions often take two years to complete. If our loan product requires adjustments, we will likely adjust this target based on market feedback on our product offering.

As we gain experience in the Section 515 market and more borrowers accept our product, we will have a greater scope and be able to better predict where these purchases will take place. Any purchases in the early years will be precedent setting and will be used to attract developer interest in the products we offer.

Challenges

There are several challenges involved in purchasing properties with USDA section 515 debt. These challenges include both external market conditions as well as necessary internal 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. The Freddie Mac loan product likely 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 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 lead to a 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 at 16,000 units per year, the market will have a well-functioning and well-tested execution in place to preserve a meaningful share of rental homes for tenants in need.

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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