

FHA's Energy Efficient Mortgages

What is an EEM

- Cost effective - the present value of the energy saved is more than the cost of the energy package (including maintenance)
- The maximum mortgage amount for an area can be exceeded by the amount of the energy package



Current Issues

- Limited traction
- Theory worked better than practice
- Fraction of total volume
- Fannie, others also limited

New Opportunities to Test New Approaches

- Congress appropriated \$50 million for testing innovative strategies for increasing role of Energy Efficient Mortgages
- HUD has signed an MOU with DOE to pilot new initiatives.
- Combination of streamlining process, ratings/audit process, consumer incentives

What is an Energy Efficient Mortgage (EEM)?

- An “add-on” to a basic FHA mortgage that allows
 - Buyers to finance energy improvements into their mortgage
 - Buyers to reduce utility bills

Background

- Started in 1993, as a pilot in 5 states -
 - Virginia, Vermont, Alaska, Arkansas and California
- In 1995, the program went national and new construction was added
- In 1998, 3-4 unit properties added

Some Details about the EEM

- A borrower can finance into an already approvable FHA loan, 100% of the cost of an eligible cost effective energy package
 - No re-appraisal needed
 - No additional qualification of borrower
 - No additional down payment is needed
- 5% of property value (up to 5 % of median appraised value)

More Details

- “Cost effective “- the present value of the energy saved is MORE than the cost of the energy package (including maintenance)
- The maximum mortgage amount for an area can be exceeded by the amount of the energy package



Theory: Benefits to Homebuyer

- More house for income
 - For a monthly income of \$4000, buyer could qualify for \$11,000 more mortgage
- Lower utility costs
 - 45% of bill is for heating and cooling
 - Energy improvements can lower bills by 20-30%
- Increased value of home?

EEM vs. EEH

- EEM is a mortgage product adding additional dollars to the loan amount.
- EEH is a house built to 2000 IECC.
- EEH allows for 'stretch ratios' when qualifying the borrower.

Energy Efficient Mortgage



- Eligibility/Requirements:
 - Existing 1- 4 unit properties and New Construction are eligible
 - Cost of the energy improvement must be “cost effective” and be less than the Present Value of the energy saved

Energy Efficient Mortgage

- EEM can be used with:
 - Section 203(h) program,
 - Section 203(b) program as purchase or refinances,
 - Section 203(k) rehabilitation,
 - Section 234(c)

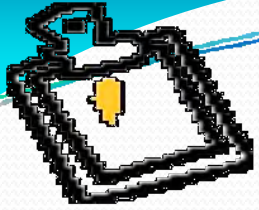


Who Can Get an EEM?

- Owner-occupants
- Non-profits

The Home Energy Rating

- An analysis of the present energy usage and the proposal of an energy package designed to improve energy efficiency.
 - A physical inspection of a house, generally including diagnostic tests.
 - A computer analysis.



- Cost of the energy improvements, including maintenance costs, and the estimate of the energy savings must be determined by a home energy ratings system (HERS) rater or energy consultant
- HERS report must be in writing and provided to the prospective borrower and lender
- Copy of the HERS report must be submitted in the case binder

The Energy Package

- A combination of energy improvements that are cost effective.
- HERS report outlines improvements, costs and energy savings.
- All items in energy package must be completed.
- Approved changes are OK if the revised energy package is still cost effective.
- Fee can be included in the Energy Package.

Loan Limits

- Statutory mortgage limit can be exceeded by the amount of the EEM.



Getting the Work Done

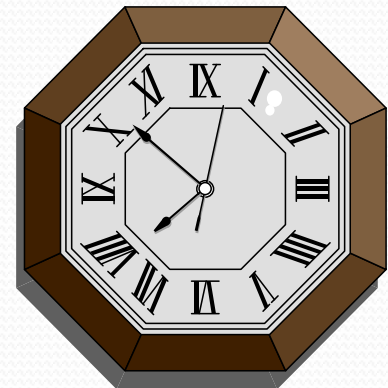
- Borrower should get bids before closing
- EEM dollars are put into a non-interest bearing escrow account - or if combined with a 203(k), put into the Rehab Escrow Account
- 90 days to complete work (6 months if a 203(k))
- Contractor cannot be Rater or HERS

Getting the Work Done

- Borrower should get bids before closing. If the bids are too high the rating may be redone.
- EEM dollars are put into escrow account - or if combined with a 203(k), put into the Rehab Escrow Account
- There is no escrow for new construction
- Contractor can't be Rater or HERS Provider

Time for Work

- Retrofit must be done within 90 days
- If combined with a 203(k), the work must be done within 180 days
- For new construction the work is completed by time of loan closing
- Post test done at completion



Steps to Get an EEM

- Buyer recognizes need to improve energy efficiency
- Buyer tells real estate agent and lender that he/she wants an EEM
- Lender makes arrangements for a Rater
- Rater does inspection/HERS Provider prepares Report
- Underwriter uses Report to make final loan calculations
- Loan closes and work is done.

Weatherization

- Mortgage amount can be increased by the cost of weatherization items
 - Cost is added to sales price and value
- Cost effectiveness is not a requirement
- Depending on the cost, an appraisal may not be required
- In some cases, weatherization may be combined with the EEM

Solar Energy Systems

- Cost of solar energy system is added directly to the mortgage amount.
- It may exceed the statutory limit by 20%.
- Amount added is the lesser of replacement cost or effect on market value.
- System can be active or passive.

EEM Facts Continued

- The mortgage is initially underwritten as if the energy package did not exist by using standard FHA underwriting guidelines and down payment requirements.
- TOTAL Scorecard may also be used for underwriting EEMs. With an “accept” or “approve” on a mortgage application, FHAC will recognize the risk rating from TOTAL and permit the increase to the mortgage amount without re-underwriting or rescoring

Calculating the maximum amount of the energy improvements

Per ML 09-18

Maximum amount of the portion of the EEM for energy improvements is the lesser of 5% of:

- The value of the property, or
- 115% of the median area price of a single family dwelling, or
- 150% of the conforming Freddie Mac limit.

UFMIP is calculated on the base mortgage amount, which includes the cost of the energy improvements.

Example using a property value of \$300,000

1st calculation – 5% of the value of the property:

$$\$300,000 \times 5\% = \$15,000$$

2nd calculation – 115% of the median area price

(use \$300,000)

$$\$300,000 \times 115\% \times 5\% = \$17,250$$

3rd calculation – 150% of conforming Freddie

Mac Limit (use \$417,000)

$$\$417,000 \times 150\% \times 5\% = \$31,275$$

Use the lesser of the 3 calculations

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Volume of EEMs

Year	New	Existing	Refi	Total
2006	145	533	183	861
2007	183	597	320	1,100
2008	208	765	262	1,235
Total	536	1,895	765	3,196

Barriers

- Lack of reliable and accessible information on such mortgages, including estimated energy savings, and other benefits of energy efficient housing;
- Confusion regarding underwriting requirements and differences among various energy efficient mortgage programs;
- The complex and time consuming process of securing such mortgages;
- Lack of automated underwriting

Barriers (cont.)

- The lack of publicly available research on the default risk of such mortgages;
- Insufficient incentives for lenders;
- Failure of home appraisals to reflect the cost of energy efficiency improvements.
- Potential secondary market pricing issues
- Underwater mortgages

Escrow Fund Efficient Mortgage

- Escrow account may be established for no more than three months after loan closing
- Escrow account must be insured and be established at a financial institution supervised by a federal agency
- If improvements are not completed in 90 days, the lender must apply funds held in escrow to the principal balance of the mortgage.

Lender disincentives

- High transaction costs
- Lack of awareness
- Escrow requirements etc.
- Don't see a connection between energy efficiency and lower risk and security

Discussion - Suggestions

- Key incentives - consumers
- Key information needs
- Key streamlining ideas
- Key incentives – lenders, realtors