

## Selling Guide Announcement SEL-2013-10

December 19, 2013

### Miscellaneous Selling Policy Updates

This Announcement describes selling policy updates that will be included in a future version of the *Selling Guide*. The effective date of each update is indicated below. The changes include:

- Margin Thresholds
- Definitions of Higher-Priced Mortgage Loan and Higher-Priced Covered Transaction
- Exceptions to Ability to Repay Rule for Certain Transactions

In addition, the following documents have also been (or will be) updated:

- *Fannie Mae Requirements for Document Custodians*
- Instructions to the *Uniform Residential Loan Application* (Form 1003)

### Margin Thresholds

In November 2012, the Treasury Market Practices Group (TMPG), an industry group sponsored by the New York Federal Reserve, issued a recommendation that forward-settling agency MBS transactions be margined in order to help manage counterparty exposures. Fannie Mae is following the TMPG's recommendation and implementing the ability to exchange bilateral margin with lenders that transact business with Fannie Mae's Capital Markets Sales Desk.

The *Selling Guide*, which currently sets forth various requirements and procedures for establishing an MBS trading account with Fannie Mae, will be updated to incorporate these recommendations. The *Selling Guide* is being updated to establish a designated threshold amount and minimum transfer amount for each lender. Subject to these amounts, a lender and Fannie Mae may exchange variation margin if there is a price differential on the lender's open (unsettled) trades with Fannie Mae.

An updated version of the applicable *Selling Guide* topic – C3-7-01, *Establishing an MBS Trading Account* – is attached to this Announcement. The blocks of text that are new or updated have been highlighted for easy reference.

### Effective Date

These changes are effective for all open trades as of January 1, 2014.

### Definitions of Higher-Priced Mortgage Loan and Higher-Priced Covered Transaction

The *Selling Guide* currently requires DU Refi Plus™ and Refi Plus™ loans that meet the “higher-priced mortgage loan” (HPML) triggers under the Truth in Lending Act/Regulation Z to have a maximum debt-to-income ratio of 45% and a minimum credit score of 620. The existing HPML provisions, however, apply only to principal residences. With the enactment of the Ability to Repay/Qualified Mortgage Rule that updated the Truth in Lending Act/Regulation Z, a new category of loans referred to as “higher-priced covered transactions” was created. This category of loans is subject to similar triggers as HPML loans but includes principal residences and second homes.

Because it was Fannie Mae's intention to apply the provisions to both principal residences and second homes, the *Selling Guide* text will be modified accordingly. *Selling Guide* topic B5-5.2-02, DU Refi Plus and Refi Plus Underwriting Considerations will be updated to reflect that if the lender determines that a loan (or Desktop Underwriter<sup>®</sup> loan casefile) is either a higher-priced mortgage loan or a higher-priced covered transaction, the loan/loan casefile must have a representative credit score of 620 or more and a debt-to-income ratio of 45% or less in order to be eligible for delivery to Fannie Mae.

In addition, two definitions will be added to the Guide:

- higher-priced covered transaction: A mortgage loan that meets the corresponding definition under Regulation Z of the Truth in Lending Act, and applies both to principal residences and second homes.
- Higher-priced mortgage loan: A mortgage loan that meets the corresponding definition under Regulation Z of the Truth in Lending Act. Only principal residences are included in this category.

### **Effective Date**

This policy is effective for all DU Refi Plus and Refi Plus mortgage applications dated on or after January 10, 2014.

## **Exceptions to Ability to Repay Rule for Certain Transactions**

In *Selling Guide* Announcement SEL-2013-07, *Selling Guide Updates*, Fannie Mae clarified the treatment of *inter vivos* revocable trust loans with respect to the ability to repay (ATR) rule.

In this Announcement, Fannie Mae is further clarifying the exception that applies not only to *inter vivos* trust loans, but also to “nonstandard mortgage” to “standard mortgage” refinance transactions. The updated exception language (as excerpted from the upcoming update to the *Selling Guide*) is as follows:

### **B2-1.4-02, Mortgage Loan Eligibility, ATR Exempt Loans**

*Exceptions:* In the following circumstances, these ATR Exempt Loans will be treated as ATR Covered Loans:

- a loan made to an *inter vivos* trust (also known as a revocable trust) that is secured by a property other than an investment property that fits within the “business purpose” definition for an exempt loan under TILA, and
- a “non-standard mortgage” to “standard mortgage” refinance transaction as defined in Regulation Z.

A loan made to an *inter vivos* trust that is secured by an investment property that fits within the “business purpose” definition for an exempt loan under TILA remains an ATR Exempt Loan.

### **Effective Date**

This policy clarification is effective for all mortgage applications dated on or after January 10, 2014.

## **Updated Requirements for Document Custodians Guide**

Fannie Mae is announcing changes to the *Requirements for Document Custodians* guide ([RDC guide](#)), which will be published on Fannie Mae's website on or before December 31, 2013. Refer to Section 1, Document Revision History, for a list and description of the updates.

## Instructions to the *Uniform Residential Loan Application (Form 1003)*

The instructions to Fannie Mae Form 1003 published on Fannie Mae's website have been updated to include the following revisions:

- clarification of entry of "net rental income";
- removal of policy pertaining to Section VIII, Declaration questions j and k regarding citizenship
  - lenders should refer to the actual policy in the *Selling Guide*;
- removal of information pertaining to the determination of first-time home buyer and how that data element is delivered to Fannie Mae
  - instructions on this element are provided in the Uniform Loan Delivery Data specifications; and
- removal of instructions that allow language to be added to Section IX, Acknowledgment and Agreement pertaining to the borrower's right to receive a copy of the appraisal report
  - effective January 18, 2014, the regulations that pertain to providing borrowers with a copy of the appraisal report are changing.

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Lenders who have questions about this Announcement should contact their Account Team.

Carlos T. Perez  
Vice President  
Chief Credit Officer for Single-Family

## Attachment

(Updated sections of the topic are highlighted.)

### **Selling Guide, C3-7-01, Establishing an MBS Trading Account**

#### **Introduction**

This topic provides information on establishing an MBS trading account, including:

- Process Used to Establish a Trading Account
- Requirements and Terms Governing the Trading Account
- Establishment of Trading Limits and Margin Requirements
- Offsetting Price Differentials
- Designated Threshold Amount and Minimum Transfer Amount
- Default of Lender Under the Terms of Trading Account
- Consequences of a Default
- Remedies for the Default of a Lender's Trading Account
- Suitability and Risk of Loss
- Transactional Intent of the Lender and Fannie Mae

#### **Process Used to Establish a Trading Account**

The table below describes the stages to establish a trading account.

Stage	Description
1	To establish a trading account, the lender may call the Capital Markets Sales Desk. See E-1-03, List of Contacts (07/30/2013).
2	Each lender must provide the following information: <ul style="list-style-type: none"> <li>▪ either a corporate resolution from its board of directors or an officer's certificate to indicate its authority to establish a trading account with the Capital Markets Sales Desk; and</li> <li>▪ the names of the designated individuals who will be authorized to sell securities to, or to buy them from, the Capital Markets Sales Desk and the limit of their authority (if any).</li> </ul>
3	Each lender must provide an address that can be used for all official notices and communications sent to the lender, and wiring instructions for the different types of payments Fannie Mae makes to the lender.
4	The lender must continue to provide updates about any changes to its authority to perform under the trading account, the individuals authorized to transact business with the Capital Markets Sales Desk (or their limits of authority), and the lender's address or wiring instructions.

## Requirements and Terms Governing the Trading Account

A lender's trading account is governed by the terms of its *Mortgage Selling and Servicing Contract* (MSSC), the provisions of this Guide and any special instructions provided for in a specific trade confirmation or settlement notice.

By initiating trade activity with the Capital Markets Sales Desk, lenders agree to adhere to Fannie Mae's guidelines for selling securities and to SIFMA's *Uniform Practices for the Clearance and Settlement of Mortgage-Backed Securities and Other Related Securities*, including any amendments to either. Should there be a conflict between the requirements in this Guide and the SIFMA provisions, the requirements of this Guide take precedence.

As security for payment of its obligations and liabilities under its trading account, the lender grants Fannie Mae a first priority security interest in any and all of its right, title, and interest in its securities, money, or other property that is held for (or by) Fannie Mae.

If appropriate authorities require the filing of a financing statement to evidence this security interest, the lender must execute and deliver any legal instruments required to protect or perfect Fannie Mae's security interest.

## Establishment of Trading Limits and Margin Requirements

When Fannie Mae establishes a trading account for a lender, it may establish trading limits, margin requirements, a designated threshold amount, and a minimum transfer amount specific to a lender.

After a trading account is established for a lender, Fannie Mae may:

- amend or cancel any trading limits, margin requirements, designated threshold amounts, or minimum transfer amounts initially imposed on a lender's trading accounts; and
- decline to engage in any specific transaction with the lender.

## Offsetting Price Differentials

Subject to the applicable designated threshold amount and minimum transfer amount (defined below), a lender and Fannie Mae may elect to exchange variation margin if there is a price differential on the lender's open (unsettled) trades with Fannie Mae.

A price differential exists if, at any time, with respect to a lender's open trades with the Capital Markets Sales Desk, either party would incur a loss if it cancelled the open trades and entered into replacement transactions (i.e., there is a difference between the current market price and the settlement price of the open trades). If a price differential exists, the party that would receive positive income from the cancellation of the open trades and entry into replacement transactions is "in the money," and the party that would incur a cost from the cancellation of the open trades and entry into replacement transactions is "out of the money."

- If there is a negative price differential for a lender's open trades with the Capital Markets Sales Desk (i.e., on any trading day, the lender is "out of the money" with regard to the securities it has contracted to purchase or sell to Fannie Mae), then Fannie Mae may request that the lender wire cash to Fannie Mae, subject to the lender's designated threshold amount and minimum transfer amount.
- If there is a positive price differential for a lender's open trades with the Capital Markets Sales Desk (i.e., on any trading day, the lender is "in the money" with regard to the securities the lender has contracted to purchase or sell to Fannie Mae), then the lender may request that Fannie Mae wire cash to the lender, subject to Fannie Mae's designated threshold amount and minimum transfer amount.

When calculating the price differential:

- any open trades between the lender and the Capital Markets Sales Desk will be disregarded if they have been assigned, submitted, transferred, or reported to a securities clearing organization (e.g., the Fixed Income Clearing Corporation) for clearing, netting, and/or settlement such that the open trade will be factored into the applicable margin requirements of such securities clearing organization; and
- any outstanding pair-off fees relating to trades between the lender and the Capital Markets Sales Desk will be factored into the calculation of the price differential.

### **Designated Threshold Amount and Minimum Transfer Amount**

The designated threshold amount represents a level of unsecured exposure an “in the money” party will accept before making a margin call on the “out of the money” party. Fannie Mae’s designated threshold amount and a lender’s designated threshold amount shall each be \$3,000,000, unless otherwise agreed to by the parties in writing and/or subject to the occurrence of a triggering event as discussed below.

Example: If there is a positive price differential and a lender is in the money by \$3,100,000, the lender may make a margin call to Fannie Mae for \$100,000. ( $\$3,100,000 - \text{Fannie Mae's designated threshold amount of } \$3,000,000$ ).

A minimum transfer is a specified amount of money that must be exceeded before a margin call can be made. Fannie Mae’s minimum transfer amount and a lender’s minimum transfer amount shall each be \$50,000, unless otherwise agreed to by the parties in writing and/or subject to the occurrence of a triggering event as discussed below.

Notwithstanding the foregoing, Fannie Mae will not wire cash to a lender in the event of a positive price differential if any of the following “triggering events” has occurred with respect to a lender:

- an event of default under the Lender Contract or any other contract between Fannie Mae and the lender,
- the lender’s failure to meet any of the lender eligibility requirements set forth in Subpart A-4, Maintaining Lender Eligibility,
- a decline in a lender’s adjusted net worth by more than 20% over a quarterly reporting period or by more than 30% over two consecutive quarterly periods,
- the total unpaid principal balance of all outstanding Fannie Mae repurchase requests to a lender exceeds 15% of the lender’s adjusted net worth,
- Fannie Mae comes into possession of information that, in Fannie Mae’s reasonable discretion, could result in an adverse impact, either presently or in the future, on the lender’s counterparty relationship with Fannie Mae or the lender’s financial condition, or
- outstanding contractual fees owed by a lender to Fannie Mae.

**Further, upon the occurrence of a triggering event for a lender, Fannie Mae, in its sole and absolute discretion, may modify or eliminate the designated threshold amount and minimum transfer amount applicable to such lender without prior notice to the lender.**

### **Default of Lender Under the Terms of Trading Account**

Under the terms of the trading account, certain events could result in the lender being in default. A lender is in default if Fannie Mae determines, at any time, that any of the representations that were made regarding the lender’s ability (or that of a designated authorized individual) to transact business is incorrect or untrue in any material respect, or if the lender:

- initiates a case or proceeding (or has a suit brought against it) under any bankruptcy, insolvency, reorganization, liquidation, dissolution, or similar law;
- seeks the appointment of a receiver, trustee, custodian, or similar official for itself or any substantial part of its property;
- executes a general assignment for the benefit of its creditors;
- admits in writing that it does not have the ability to pay its debts as they come due;
- is subject to an outstanding, uncontested order of relief or a protective decree issued under the Securities Investor Protection Act; or
- fails to perform as required. Instances of nonperformance that constitute a default include the failure to:
  - perform any of the obligations set out in a confirmation or settlement notice;
  - perform any obligations with respect to completing a trade (or the admission that it is unable or unwilling to do so);
  - perform obligations under any other agreement or contract it has with Fannie Mae;
  - if notice is sent by Fannie Mae by 10:00 a.m. on a business day, satisfy the price differential on lender's trades with the Capital Markets Sales Desk by the close of business on that same business day; or
  - if notice is sent by Fannie Mae after 10:00 a.m. on a business day, satisfy the price differential on lender's trades with the Capital Markets Sales Desk by 12:00 noon on the next business day.

### Consequences of a Default

A default with respect to one transaction will constitute a default for all of the lender's transactions with the Capital Markets Sales Desk. See E-1-03, List of Contacts (07/30/2013).

Lender's payments, deliveries, and transfers for one transaction may be applied ("netted") against lender's other transactions.

Fannie Mae also may treat a default under the lender's trading account as a default under the lender's MSSC.

When that is the case, the provisions for "termination (of a selling or servicing arrangement or the contract) for cause" that are set out in A2-3.1-01, Lender Breach of Contract (04/09/2013), will apply.

### Remedies for the Default of a Lender's Trading Account

The lender will be liable for any losses Fannie Mae incurs due to the lender's default with the Capital Markets Sales Desk. See E-1-03, List of Contacts (07/30/2013). The following table details the remedies that are available to Fannie Mae when it declares a lender to be in default under its trading account:

If ...	Then ...
Fannie Mae declares a lender to be in default under its trading account,	Fannie Mae may require that the settlement for all of the lender's outstanding transactions be accelerated and take place immediately. In addition, Fannie Mae shall have all rights and remedies of a secured party under the Uniform Commercial Code and any other rights available under applicable law.
The lender was committed to buy securities from	Fannie Mae may sell the securities at the current

the Capital Markets Sales Desk,	market value (or, as an alternative, give the lender credit for the current market value as if a sale had taken place). The lender will then be liable for any loss that occurs because the current market value is less than the purchase price the lender would have paid had the securities been transferred to it.
The lender was committed to sell securities to the Capital Markets Sales Desk,	Fannie Mae may purchase securities of the same class and amount as those the lender was committed to sell at the current market value (or, as an alternative, deem itself to have purchased the comparable securities for the purpose of determining the lender's liability). The lender will then be liable for any loss that occurs because the current market value is greater than the purchase price Fannie Mae would have paid had the lender transferred the securities to the Capital Markets Sales Desk.

In addition, the lender must pay:

- all reasonable legal and other expenses Fannie Mae incurs in connection with, or as the result of, the lender's default under its trading account, and
- interest on the losses and expenses for which the lender is liable from the date of default to the date the lender reimburses Fannie Mae.

**Note:** *The interest charged will be based upon the prime rate for commercial banks that is published in The Wall Street Journal.*

If necessary, Fannie Mae may liquidate and apply against the obligations the lender owes as the result of its default, any and all of the lender's securities, money, and other property that is held for (or by) Fannie Mae.

### Suitability and Risk of Loss

The risk of loss when transacting with the Capital Market Sales Desk can be substantial. A lender should carefully consider whether a transaction is suitable in light of its financial condition, its investment objectives, and any legal or regulatory restrictions to which it may be subject. The market value for the securities to be purchased or sold by a lender can vary substantially over the term of a transaction. A lender should carefully consider if it has the operational resources in place to monitor the risks and contractual obligations of a transaction, including the risk that Fannie Mae may request that a lender post margin to satisfy a price differential on the same or the following business day.

By agreeing to a confirmation, the lender is deemed to have represented and warranted that it understands the risks associated with the transaction with the Capital Market Sales Desk, and the lender believes that the transaction is suitable for the lender. Similarly, to the extent that the lender assigns or transfers any of its rights and obligations under any transaction, the lender shall be deemed to represent and warrant as of the date of such assignment that the lender has reasonable grounds to believe that any such assigned transaction is a suitable transaction for the assignee. Fannie Mae and the lender agree that, if any rights and obligations are so assigned by the lender, notwithstanding any consent to such assignment by Fannie Mae, Fannie Mae shall have no obligation to undertake an evaluation of the suitability of the assigned rights and obligations to the assignee.



Before engaging in any transactions with the Capital Market Sales Desk, a lender should consult its own business, legal, tax, risk, accounting, and other advisers and examine the provisions in this Chapter of the Guide to determine whether the risks to the lender are appropriate.

### **Transactional Intent of the Lender and Fannie Mae**

The lender acknowledges, at all times, that Fannie Mae is not acting as a fiduciary or an advisor with respect to any transaction with the Capital Market Sales Desk.

The lender and Fannie Mae also agree that transactions between the lender and the Capital Market Sales Desk are intended to be:

- “forward contracts,” “securities contracts, and “master netting agreements,” as the term is defined in Section 741 of Title 11 of the United States Code, as amended; as such terms are defined in the United States Bankruptcy Code, as amended, and of a type set forth in Section 5390(c)(8)(D) or Title 12, as amended;
- “qualified financial contracts,” if the lender is an “insured depository institution” under the Federal Deposit Insurance Act, as amended; and
- a “netting contract” as defined in and subject to Title IV of the Federal Deposit Insurance Corporation Improvement Act of 1991, as amended, and each payment entitlement and payment obligation under any transaction shall constitute a “covered contractual payment entitlement” or “covered contractual payment obligation, respectively, as such terms are defined in such Act.

The lender and Fannie Mae also agree that either party’s rights to cancel a transaction or exercise any other remedies upon a default is a contractual right to liquidate such transaction as described in Section 555 and 556 of the United States Bankruptcy Code, as amended, and a right to terminate, liquidate, or accelerate as described in Sections 5390(c)(8)(A) and (C) of Title 12 of the United States Code, as amended.