



Fannie Mae Training: Changes to the Structured Adjustable-Rate Mortgage Loan (SARM)

October 2024



Agenda



**New SARM
Changes**



**Benefits and
Features**



**Underwriting
and Post-
Closing**



**Submitting and
Delivery**



SARM Enhancements and Changes



Strengthening the SARM

Maintain a strong variable rate product and meet the market for Fannie Mae's most used variable-rate loan product.



Enhancements and Changes

Summary

Changes	New SARM Parameters	Existing SARM Parameters
Streamlined UPB Calcs	4 U/W Tests	5 U/W Tests
Tier 2 DSCR	Refer to Form 4660	Refer to Form 4660
Tier 2 LTV	Refer to Form 4660	Refer to Form 4660
Loan Term	5 year	5, 7 and 10 years
Interest-Rate Cap Term	5 year	3-5 year
Replacement Interest-Rate Cap Escrow (when applicable)	<ul style="list-style-type: none">• Escrow fully funded at 110% at closing• Release of excess funds is allowed	<ul style="list-style-type: none">• Funded monthly over the original cap term• No release of excess escrow funds

Note: These terms are applicable to DUS Flow loans, Structured Transactions have different tolerances on max LTV, loan term, and cap term.



U/W Tests and Max. Note Rate

New SARM Parameters	Existing SARM Parameters
1. Fixed Rate Test	1. Fixed Rate Test
2. Max LTV Test	2. Max LTV Test
3. Max Note Rate Test	3. Variable UW Rate Test
4. Pay Rate Test	4. Min Strike Test
	5. Pay Rate Test

Max Note Rate = Minimum Cap Strike Rate
G + S Fee
Investor Spread

Minimum Cap Strike Rate is set by Fannie Mae and reviewed every quarter at a minimum.



Loan Term and Sizing

Product Type Considerations

Conventional & MAH

- SARM loans will be quoted with a 5-year term

Structured Transactions

- SARM Loans may have terms up to 7 and 10 years for certain product types

Sizing by Tier

TIER	Min UW DSCR	Max LTV (Conv.)	Max LTV (MAH)
2	Refer to Form 4660		
3	Refer to Form 4660		
4	Refer to Form 4660		

*Refer to the latest Form 4660 for current DSCR/LTV requirements



Interest Rate Caps

DUS Flow Loans

5 year
loan term



5 year
cap term



**New: Loan Term must
match cap term**



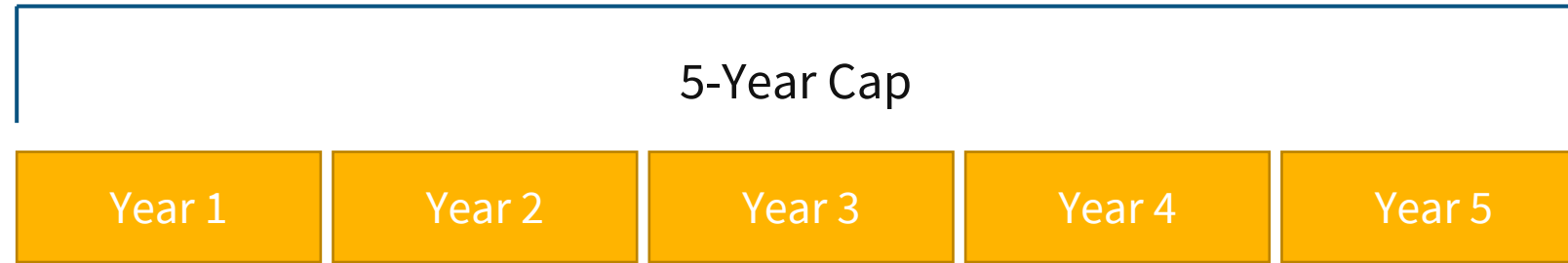
**No replacement cap
escrow required**



Interest Rate Caps

DUS Flow Loans

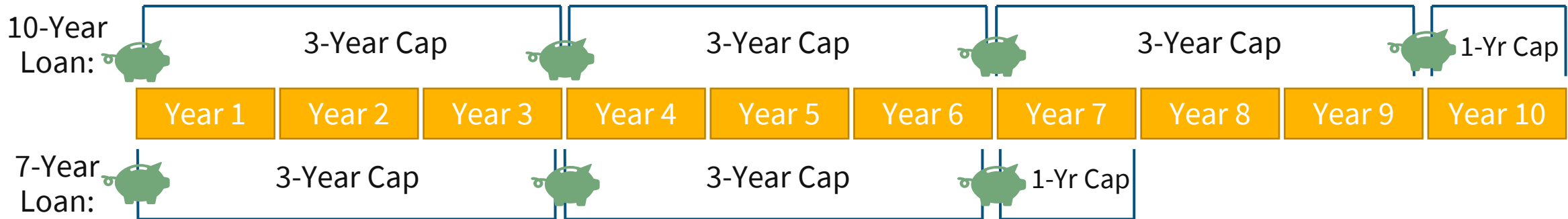
5-Year Loan:



Interest Rate Caps

Structured Transactions

These requirements apply to loans with an initial interest rate cap that will mature before the SARM loan matures



Escrow



Funds Replacement Cap

Escrows for replacement caps cannot be held for a longer than 36 months.



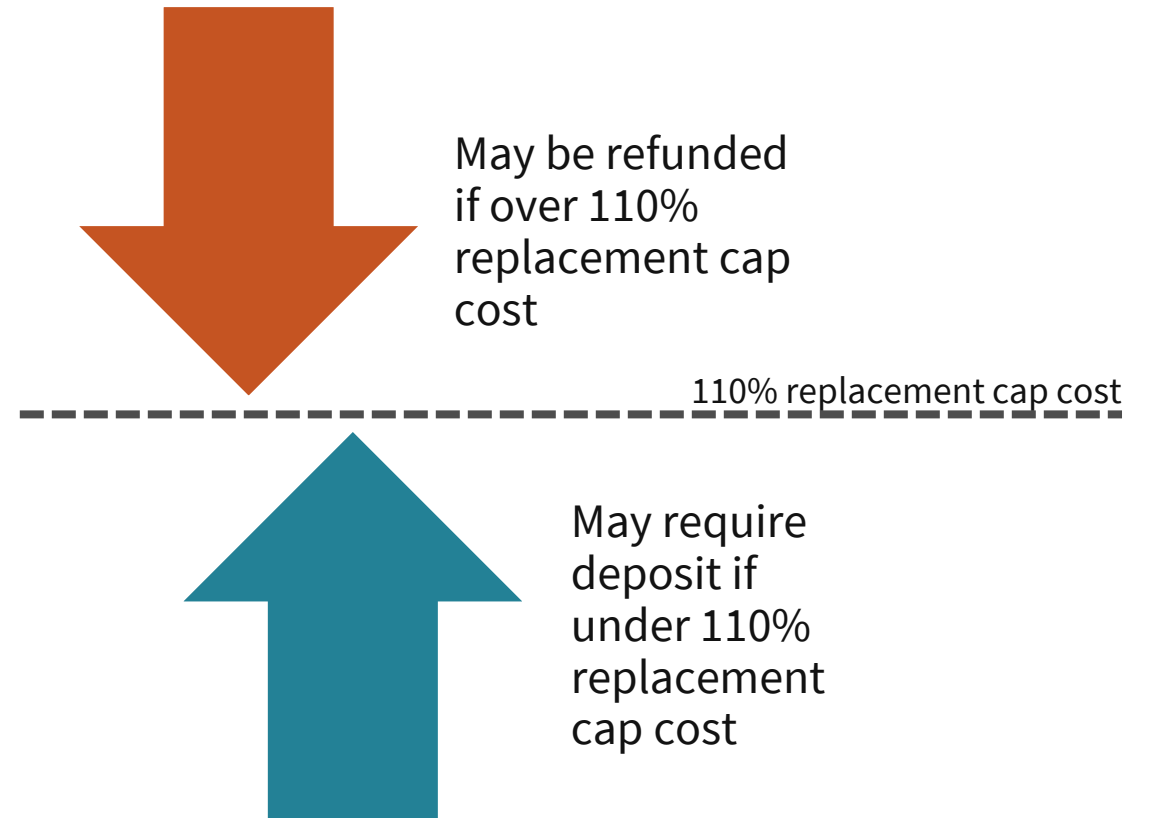
Replacement Cap Escrows

Escrows are required to be funded at 110% of replacement cost over the life of the interest rate cap

Are the escrows ever adjusted?



Replacement cap escrows are adjusted or resized every six months relative to replacement cap costs. We now allow escrows to be adjusted up or down.



Benefits and Eligibility



SARM Eligibility



Loan Size

\$25 Million minimum



Borrower

Has prior experience with interest rate hedges



Interest Rate Cap

- External cap required
- [Fannie Mae approved provider](#)



Asset Types

- All are eligible
- Some require additional approval



SARM Terms

Loan Size
\$25 Million minimum

Terms:
5 years
(conventional)

Asset Types
All (some require approval)

Accrual
Actual 360
Amortization
Straight-line

LTV/ DSCR:
Tier 2: Form 4660
Tier 3: Form 4660
Tier 4: Form 4660

Pre-Review?
Yes

Conversion
Option to convert to
a fixed-rate loan

SOFR Index
30-Day Average

Prepayment
1% prepay or
declining prepay



SARM Loans Offer Flexibility

If your Borrower is...	Feature
Considering a shorter holding period	Ability to prepay: After a 1-year lockout, a 1% Prepayment Premium applies
Considering converting to a fixed-rate Mortgage Loan in the future	Mortgage Loan may be converted to fixed-interest rate starting in Year 2
Considering trends in interest rate movement	Take advantage of variable rate and benefit when interest rates decrease during loan term



Prepay Options - Flexible Exits

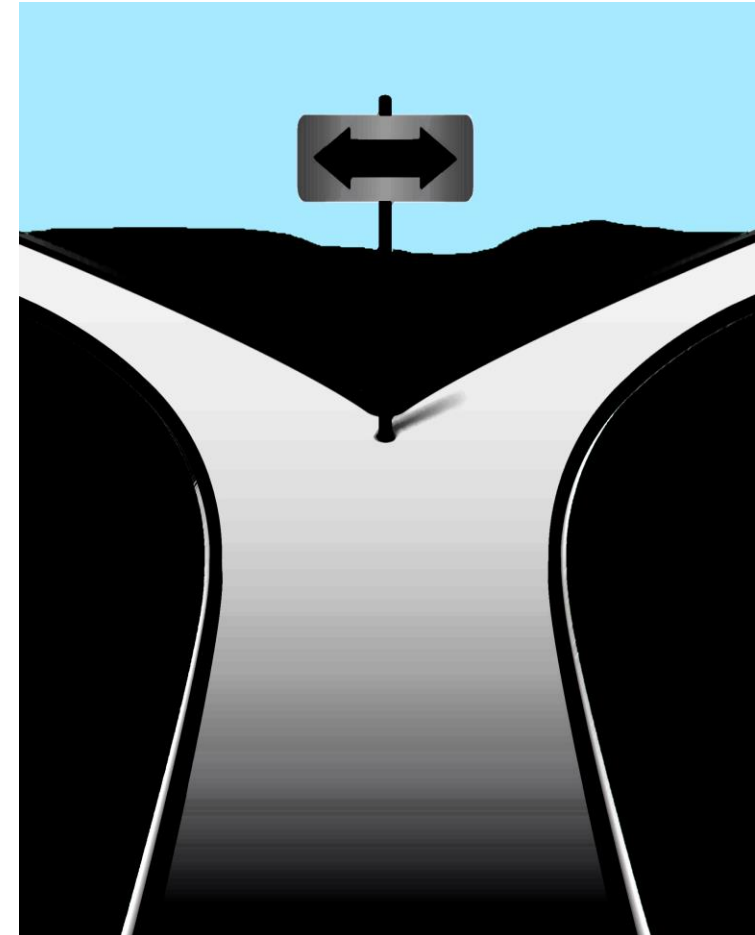
SARM Loans offers multiple flexible options for Borrowers depending on circumstances

Prepayment Flexibility

1% Prepayment Premium option
1 year lockout; then 1% Prepayment Premium

Declining Prepayment Premium option
1 year lockout, then declining Prepayment Premium (4%, 3%, 2%, and 1% thereafter)

No Prepayment Premium during last 3 months of the loan term



Term Options – Convert to Fixed

Conversion to Fixed-Rate

Timing: Any rate change date beginning with the first day of the second Loan Year and ending on the first day of the third month prior to the Mortgage Loan Maturity Date

Options: 5, 7, or 10 year fixed-rate loan terms

Pricing: G&S fees generally require use of current fixed-rate pricing grid; some allow the original G&S fees.

Premium: Lender can take a 25 bp premium on the trade of the MBS securitized by the new fixed-rate Mortgage Loan

Loan Amount: No increase in loan amount at time of conversion; additional proceeds may be funded with a Supplemental Mortgage Loan

- ✓ **No prepayment penalty at conversion**
- ✓ **Minimal re-underwriting required**
- ✓ **Amortization schedule can be “Re-set” to 30 years**



Underwriting & Post-Closing



Determining the Loan Amount

Loan Amount is the lower of:

- 1. Fixed Rate Test:** Requires that the loan amount for a variable rate transaction be the same as or less than a comparable fixed rate transaction.
- 2. Max LTV Test:** UPB that results from using the applicable LTV standards for SARMs
- 3. Max Note Rate Test:** UPB that results from the max note rate (**Minimum Cap Strike Rate** + Investor Spread + Gfee + Sfee) at the minimum UW DSCR using the applicable standard for SARMs
- 4. Pay Rate Test:** UPB that results from the pay rate (Index + Investor Spread + Gfee + Sfee) at the minimum amortizing DSCR for the fixed rate equivalent.

Minimum Cap Strike Rate:

- Minimum Cap Strike Rate is an underwriting rate set by Fannie Mae and adjusted periodically based on market conditions.
- Fannie Mae currently (October 2024) requires a minimum 7.50% Cap Strike Rate.



Straight Line Amortization

- **SARM amortization mirrors a comparable fixed rate deal.**
- You must obtain a fixed rate quote when SARM is quoted.
- Payments are flat across all amortization months.



Why a Cap?

Understanding the impact of a variable rate Mortgage Loan without an embedded cap

What are interest rate caps?



An interest rate cap is a financial instrument that gives the Borrower protection from large interest rate increases. The cap buyer receives payments at the end of each period in which the interest rate exceeds the agreed strike price.



A loan without a rate cap is exposed to market volatility.



To reduce interest rate risk, Fannie Mae requires the Borrower to purchase an interest rate cap for all SARM Loans.



Interest Rate Cap Management

New requirements are shown in blue

Origination/Structuring

- Engage Cap Broker
- Purchase cap from approved provider
- Cap index: 30-Day Average SOFR

Commitment/Delivery

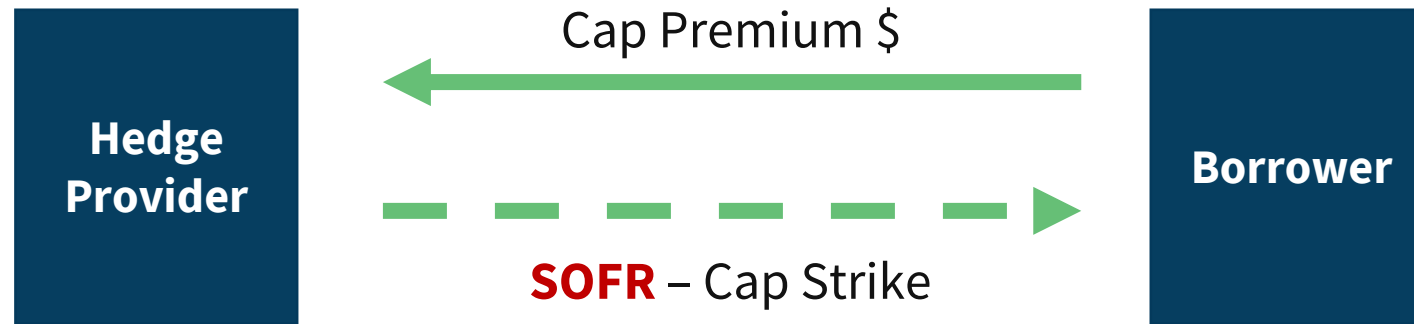
- Cap purchased
- **Escrow funding at 110% of replacement cost**

Post Closing

- Cap in place
- Escrow for replacement cap (if required)
- **Replacement cap escrow cannot be held longer than 36 months**
- **Replacement cap costs can be adjusted upward or downward every 6 months**



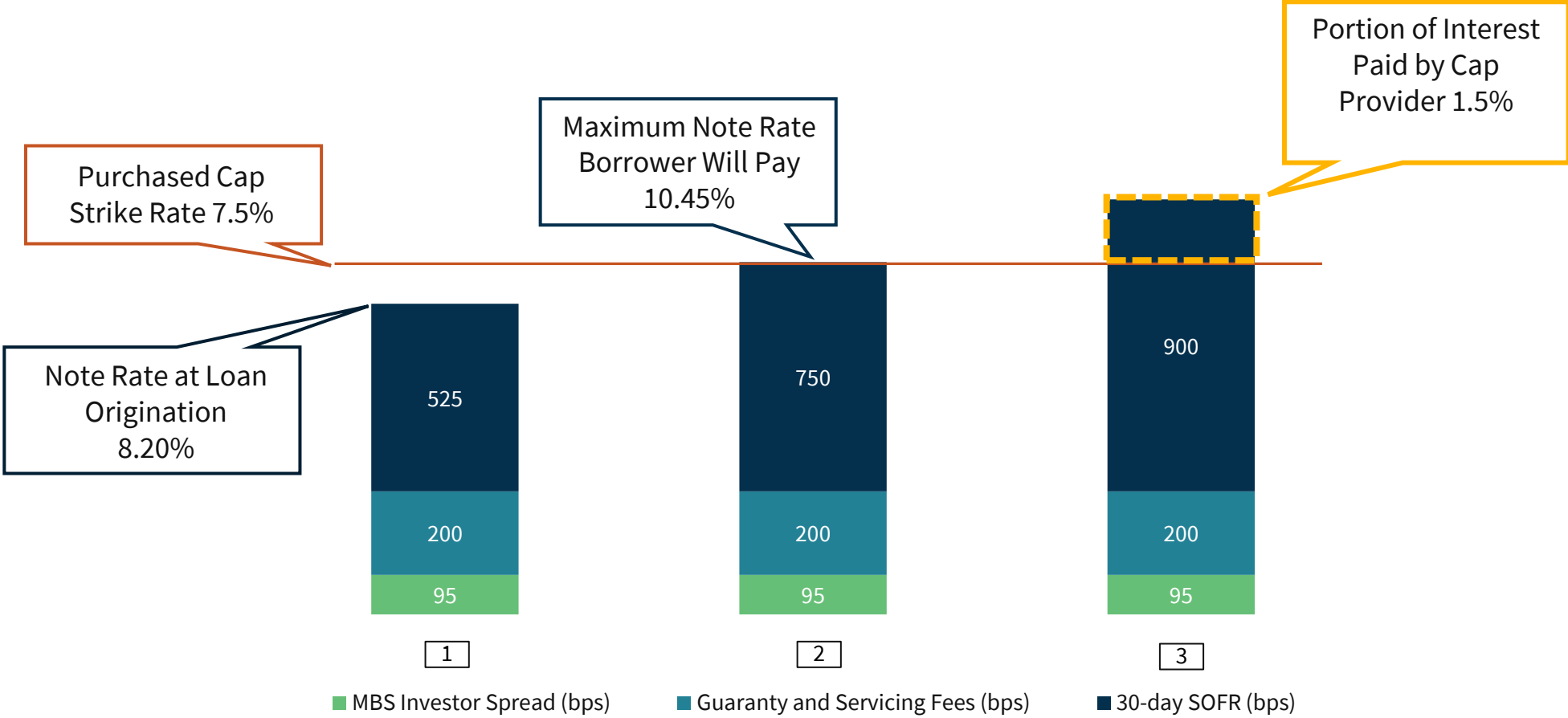
Cap Payments + Flow of Funds



- The Borrower is responsible for purchasing the cap prior to Mortgage Loan Delivery
- Borrower's net upfront payment = Cap Premium
- Borrower's net ongoing interest payment = Lesser of 30-Day Average SOFR or Cap Strike Rate + Margin (Investor + G + S)
- Hedge Provider's interest payment = 30-Day Average SOFR - Cap Strike (only applies when 30-Day Average SOFR > Cap Strike Rate)



How Do Interest Rate Caps Work?



Changes to DUS[®] Gateway



Submission and Commitment

Changes	New SARM Parameters	Existing SARM Parameters
DUS Gateway Requirements	Lender enters SARM Underwritten Cap Strike Rate field (new)	Lender enters Underwritten Stress / Max Lifetime Pass Through Rate
	Max Note Rate field (new) will be calculated by Gateway	Underwritten Variable / Max Lifetime Interest Rate is used
	Max Note Rate Constant field (new) will be calculated by Gateway	Underwritten Variable / Max Lifetime Rate Loan Constant is used



Registration in DUS[®] Gateway

New Loan Option Input Requirements

- In DUS[®] Gateway, Variable Rate Interest, enter
 - SARM Underwritten Cap Strike Rate (ask your Fannie Mae deal team)
 - Max Note Rate
 - Max Note Rate Loan Constant is a new field that will be populated by DUS[®] Gateway

Loan Options (5) <input type="checkbox"/> Select All	LO1083303 <input type="checkbox"/> ACTIVE
Actions ▼ Expand All Collapse All Collapse Summary ↑	
Rec Non-Green Variable Rate (SARM) Tier 2 60mo. Prepayment Lockout 12mo. 1% Fixed Prepayment 57mo. No Prepayment (Open) 60mo. 60mo. 65% 1.25 100% \$23.18 MM	
▼ VARIABLE RATE INTEREST	
Index Rate Type	30 Day Average SOFR
Index Rate	5.330%
Total Variable Rate Investor Spread	0.600%
Variable Rate Guaranty Fee	0.960%
Variable Rate Servicing Fee	0.640%
Cap Cost Factor	0.000%
Actual Variable Interest Rate	7.530%
SARM UW Cap Strike Rate	7.500%
Max Note Rate	9.700%
UW Stress / Max Lifetime Pass Thr...	6.000%
UW Variable / Max Lifetime Intere...	



DUS Gateway Demo

