U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-8000

OFFICE OF HOUSING

SEP 30 2005

Ms. Pamela F. Banks
Vice President
Regulatory Compliance
Fannie Mae
3900 Wisconsin Avenue, NW
Washington, DC 20016-2892

Dear Ms. Banks:

By letter to the Department dated March 1, 2005, Fannie Mae requested an interpretation from the Department of the rules governing the calculation, for housing goals purposes, of purchases and guarantees of portions of real estate mortgage investment conduits (REMICs). Fannie Mae seeks this interpretation in the context of calculating partial housing goals credit for its purchase and guarantee of securities issued by REMIC structures where the mortgage collateral backing the securities is divided into discrete bond groups. The securities related to one or more of the bond groups in these REMICs are backed by conventional conforming mortgages or other mortgages eligible for purchase by Fannie Mae while the securities relating to other bond groups in the REMIC are backed by non-conforming mortgages or by non-residential mortgages. REMICs structured in this manner with mixed collateral bond groups are referred to in this letter guidance as "directed-pay tranche" REMICs, as that term is more specifically defined herein.

HUD's regulations at 24 CFR 81.16(c)(2)(ii)(B) do not provide guidance to the GSEs on how to calculate housing goal credit for their purchase/guarantee of a portion of the securities issued by a mixed-collateral directed-pay tranche REMIC. Rather, HUD's rule envisioned classes of REMIC transactions with a single bond group where the assets of the whole REMIC are eligible for purchase/guarantee by a GSE and where partial housing goal credit is based on the GSE's percentage of participation in the whole REMIC.

HUD's regulations at 24 CFR 81.16(d) authorize HUD to determine whether a class of transactions that does not otherwise count under the rules in 24 CFR part 81 counts as a "mortgage purchase" and the extent to which this class of transactions may count toward the housing goals. This provision is consistent with section 1336(a)(2) of the Federal Housing Enterprises Financial Safety and Soundness Act of 1992 (FHEFSSA), which authorizes the Secretary to establish guidelines to measure the extent of compliance with the housing goals and to assign full, partial, or no credit toward achievement of the housing goals to different categories of GSE mortgage purchase activities based on such criteria as the Secretary deems appropriate.

Pursuant to these authorities, the Department has reviewed the mixed-collateral directed-pay tranche REMIC structures with discrete bond groups, as described in Fannie Mae's letter of March 1, and has determined that:

(1) Directed-pay tranche REMICs represent a new class of REMIC transactions that do not otherwise count under the rules in 24 CFR part 81, including the existing REMIC counting rules at 24 CFR 81.16(c)(2)(ii)(B);

(2) Fannie Mae's purchase/guarantee of securities issued against one or more bond groups collateralized by conforming mortgages or other eligible mortgages in a mixed-collateral, directed-pay tranche REMIC, and that otherwise satisfy the requirements set forth in paragraphs (a) and (b) of this letter guidance, shall be treated as a "mortgage purchase" pursuant to 24 CFR 81.16(a) because HUD has determined that this activity adds liquidity to the existing REMIC market; and

(3) A mortgage purchase that satisfies the requirements in paragraph (2), above, shall count toward Fannie Mae's housing goals according to the formula described in paragraph (c) of this letter guidance, provided, however, that such mortgage purchase must actually fulfill Fannie Mae's purposes and be in accordance with its Charter Act, as required by 24 CFR 81.16(a).

By this letter, the Department is providing Fannie Mae with guidance on how to calculate partial credit when Fannie Mae purchases/guarantees securities issued against one or more bond groups collateralized by conforming mortgages or other eligible mortgages within a mixed-collateral, directed-pay tranche REMIC, but not the whole REMIC. This guidance, which is applicable to both single-family and multifamily REMIC structures with directed-pay tranches, is effective immediately for all current year mortgage purchases beginning with January 1, 2005.

(a) <u>Definition</u>: This guidance authorizes Fannie Mae to count as a mortgage purchase toward the housing goals, in accordance with the formula in paragraph (c), its purchase/guarantee of securities issued against one or more bond groups in a REMIC securitized by both conforming mortgages or other eligible mortgages and nonconforming or non-residential mortgages where:

(1) Mortgage loans are assigned to discrete bond groups for each class of security issued;

(2) Mortgage cash flows derived from the collateral backing each bond group and class of security are distributed to investors who purchase the securities for the corresponding bond group;

(3) Subordinate tranche(s) that receive cash flows from all bond groups in the REMIC provide credit enhancement for senior REMIC tranches; and

(4) An investor in a senior tranche within the REMIC is entitled to the mortgage cash flows derived only from the collateral backing the class of certificate purchased.

These REMIC structures are referred to in this letter guidance as "directed-pay tranche" REMICs. These structures allow a GSE to purchase/guarantee specific conforming mortgages or other eligible mortgages of a REMIC rather than all of the mortgages of the whole REMIC.

(b) Exclusions: The Department will permit Fannie Mae to use the formula in paragraph (c) of this guidance for purposes of counting dwelling units derived from its purchase/guarantee of a specific bond group in a mixed collateral, directed-pay tranche REMIC, rather than the whole REMIC, provided:

(1) The general requirements of 24 CFR 81.16(c)(2)(i) for the counting of units financed by a REMIC structure are satisfied;

(2) None of the collateral associated with the whole REMIC, including all groups of mortgages, is backed by mortgages originated or sold contrary to good lending practices, or consists of HOEPA mortgages and mortgages with unacceptable terms and conditions, as defined in 24 CFR 81.2; and

(3) The security is a senior, investment-grade tranche.

(c) Instructions for Calculating Partial REMIC Housing Goal Credit:

(1) **General rule.** For directed-pay tranche REMICs that meet the requirements in paragraphs (a) and (b) of this letter guidance, and for which Fannie Mae purchases/guarantees some or all of the REMIC certificates issued by a senior investment-grade tranche backed by conforming mortgages or other eligible mortgages in the REMIC, Fannie Mae shall receive partial credit toward achievement of the housing goals.

(2) **Numerator.** The partial credit referred to in paragraph (c)(1) shall be equal to: a ratio calculated as the sum of the dollar value of the bond group in which Fannie Mae has acquired a whole or partial interest (A) and the dollar value of all other bond groups (B), divided by the sum of the values of all the bond groups and all subordinate tranches (A+B+C), multiplied by a ratio calculated as the dollar value of the GSE's interest (G) divided by the total dollar value of the REMIC certificate in which the GSE acquired an interest (A). (If the GSE acquires an interest in all of the REMIC certificates, the latter ratio will be "1".) The product of the two ratios is multiplied by the number of dwelling units financed by the REMIC certificate in which the GSE acquired an interest and which

qualify to count towards a housing goal ($U_{A,Q}$). Thus, the numerator is

$$n = [(A + B)/ (A + B + C)] \times (G/A) \times U_{A,Q}$$

EXAMPLE: In a directed-pay tranche REMIC, assume that the whole REMIC has a value of $100 million and that "A", "B", "C" and "G" (as those terms are defined in paragraph (c)(2)) have the following values:

- "A" is $30 million, representing the value of a bond group collateralized by propert(ies) representing 600 dwelling units.
- "G" is $15 million, representing the value of the GSE's investment in the bond group.
- "$U_{A,Q}$" is 250 units, which is the portion of the 600 units that qualify for the housing goal, for example, the low-and moderate-income housing goal.
- "B" has a value of $50 million.
- "C" has a value of $20 million.

Based upon these figures, the number of units that should be included in the numerator under paragraphs (c)(2) is determined as follows:

APPLICATION OF FORMULA TO FACTS:

$$n = [(30 + 50) / (30 + 50 + 20)] \times (15/30) \times 250$$

$$n = [0.8] \times [0.5] \times 250$$

$$n = 0.4 \times 250$$

n = 100 units to be included in the low/mod numerator

(3) **Denominator.** To calculate the number of units to be included in the housing goals denominator, apply the same formula used to calculate the numerator under paragraph (c)(2), except that the final result is multiplied by the total number of dwelling units that are eligible to count toward a goal under section 81.15(a)(2) and which are financed by the REMIC certificate in which the GSE acquired an interest (U_A). Thus, the value of the denominator is

$$d = [(A + B) / (A + B + C)] \times (G/A) \times U_A$$

EXAMPLE: Using the same assumptions described above for calculating the numerator, calculate the denominator as follows:

APPLICATION OF FORMULA TO FACTS:

$d = [(30 + 50) / (30 + 50 + 20)] \times (15/30) \times 600$

$d = [0.8] \times [0.5] \times 600$ units

$d = 0.4 \times 600$ units

$d = 240$ units to be included in low/mod denominator

Should you have any questions about the guidance provided herein, please do not hesitate to call me.

Sincerely,

Sandra L. Fostek

Sandra L. Fostek
Director
Office of Government Sponsored
Enterprises Oversight