



TO: Freddie Mac Sellers and Servicers

October 7, 2015 | 2015-17

SUBJECT: SELLING REPRESENTATION AND WARRANTY FRAMEWORK – ORIGATION DEFECTS AND REMEDIES

Freddie Mac, jointly with Fannie Mae, at the direction of the Federal Housing Finance Agency (FHFA), is pleased to announce the selling representation and warranty framework – origination defects and remedies (the “remedies framework”). The remedies framework expands upon provisions contained in the selling representation and warranty framework (introduced in *Single Family Seller/Service Guide* (“Guide”) Bulletin 2012-18, and subsequently updated in Bulletins 2014-8 and 2014-21) specifically related to corrections of identified origination defects, and available repurchase alternatives. The remedies framework provides clarity on the process followed in categorizing origination defects, Seller corrections of such defects and available remedies. In addition, it provides more transparency regarding Freddie Mac’s discretion on loan-level decisions when reviewing a Mortgage in quality control. The remedies framework does not affect any Servicing representations and warranties.

In adopting the remedies framework, we are not discharging Sellers from responsibility for underwriting and delivering investment quality Mortgages in accordance with the terms of the Purchase Documents.

EFFECTIVE DATE

The remedies framework is effective for Mortgages with Freddie Mac Settlement Dates on and after January 1, 2016.

BACKGROUND

While the mortgage industry has undergone significant changes in the last few years, selling representations and warranties continue to remain important by promoting liquidity and providing the necessary assurances that allow Freddie Mac to purchase Mortgages in an efficient and responsible manner without reviewing each Mortgage individually when it is sold to Freddie Mac. They also provide Freddie Mac with remedies to address situations where a Seller/Service’s obligations to meet the requirements of its Purchase Documents have not been met.

Over the last several years, Freddie Mac and Fannie Mae, at the direction of FHFA, have worked to refine the selling representation and warranty framework. As part of this process, we have listened closely to concerns about the impact that Mortgage repurchases have had on business. We understand the need to address these concerns in ways that are mutually satisfactory to ensure that there is liquidity in the housing finance market and to provide access to credit for Borrowers. Through the introduction of the remedies framework, Freddie Mac and Fannie Mae are working to provide clarity and transparency regarding origination defects and remedies, and expect these changes will enable Seller/Service’s to manage risk more effectively.

OVERVIEW

After completing a full-file quality control review, Freddie Mac will categorize defects in one of three ways:

- Findings
- Price-adjusted loans, and
- Significant defects

Mortgages with defects categorized as “Findings” will not require a Correction or a Remedy (as defined below) from the Seller. Loans categorized as “Price-Adjusted Loans” require the Seller to pay the applicable post-settlement delivery fee (“delivery fee”) that should have been paid to Freddie Mac when the Mortgage was delivered. If a Mortgage has one or more defects categorized as a “Significant Defect,” Freddie Mac will require the repurchase of the Mortgage, or may offer the Seller/Service a repurchase alternative.

At any time during the appeals process, the Seller/Servicer will have the right to correct any Significant Defect (as defined below) in the specified time frame and in the manner required by the Purchase Documents. If the Significant Defect is corrected in accordance with the terms of the Purchase Documents, Freddie Mac will rescind the related remedy request.

DEFINITIONS

In support of the remedies framework, the following terms will be added to Guide Section 46.1:

- **Correction:** Action taken by the Seller/Servicer, typically through delivery of documentation or information to Freddie Mac, that demonstrates that the identified Significant Defect (i) did not, in fact, exist at the time of Mortgage purchase, or (ii) has been corrected in the time frame and manner specified in the Purchase Documents such that the Defect is no longer considered by Freddie Mac to be a Significant Defect. Examples of Corrections include, but are not limited to, De Minimis Corrections and the acquisition of required insurance.
- **Counterparty Status:** Freddie Mac's assessment of a Seller/Servicer's financial capacity which could determine which Remedy Freddie Mac will offer to a Seller/Servicer for a Mortgage with a Significant Defect
- **Defect:** A loan-level deficiency that breaches a term contained in the Purchase Documents in effect at the time of Mortgage purchase
- **De Minimis Correction:** Minor amount not to exceed \$500 (or such higher amount as the Seller/Servicer and Freddie Mac may agree) that, when remitted, refunded, or otherwise provided, corrects or otherwise resolves an identified Significant Defect. A De Minimis Correction cannot be made: (a) in connection with any Mortgage where the correction would result in a specific required minimum Borrower contribution not being met; or (b) to correct a violation of the requirements set forth in the Freddie Mac Charter Act
- **Finding:** One or more Defects that, when considered with other Mortgage features, does not necessitate a change in the price of the Mortgage or result in the Mortgage being unacceptable even if the true and accurate facts about the Mortgage had been known at the time Freddie Mac acquired the Mortgage
- **Price-Adjusted Loan ("PAL"):** One or more Defects that, when considered with other Mortgage features, and based on the facts of the Mortgage as delivered to Freddie Mac, result in a Mortgage that was otherwise eligible for delivery to Freddie Mac had the correct data been delivered and postsettlement delivery fee (delivery fee) been paid to Freddie Mac by the Seller/Servicer
- **Remedy:** An action to resolve a Significant Defect elected by Freddie Mac pursuant to the Purchase Documents in effect at the time of Mortgage purchase
- **Repurchase Alternative:** Remedies other than repurchase of the identified Mortgage. Repurchase Alternatives could include, but are not limited to:

Performing Loans	Non-Performing Loans
Recourse/repurchase agreement	Make-whole payment
Indemnification agreement	Split loss
Mortgage insurance stand-in agreement	Loss reimbursement
Collateralized indemnification agreements (collateral in lieu of repurchase or collateralized recourse)	

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- **Significant Defect:** One or more Defects that either necessitate a change to the price on which the Mortgage was acquired or result in the Mortgage being unacceptable for purchase had the true and accurate information about the Mortgage been known at time of purchase. Mortgages with Findings and PALs are not Mortgages with Significant Defects.

In determining whether there is a Significant Defect, Freddie Mac must give due consideration to the severity of the Defect. In addition, in order to be a Significant Defect, the Defect must relate to one of the following:

- (a) The underwriting of the Borrower's creditworthiness and capacity (e.g., Borrower's income, Borrower credit/liabilities, and Borrower assets) or Borrower eligibility and qualification (e.g., area median income, First-Time Homebuyer, lawful presence in the United States)
- (b) The underwriting criteria related to property or project eligibility (e.g., residential use and condo eligibility), the property appraisal, or the physical condition of the property
- (c) Mortgage or product terms and criteria (e.g., products that may require special lender approval as a prerequisite for delivery and the criteria described in the Purchase Documents such as loan-to-value (LTV) ratio, occupancy, credit score, loan purpose, and loan product and terms such as ineligible transaction types and limitations on cash out to the Borrower that determines the type of refinance) or any terms and criteria set forth in any negotiated provision)
- (d) A life-of-loan representation and warranty (as described in Section 6.14(c))
- (e) Requirements applicable at time of Mortgage purchase (e.g., no defaults, all taxes and insurances have been paid or escrows established and no modification, encumbrance, subordination or release of Mortgage)
- (f) The warranties and obligations of Seller/Servicer regarding the Freddie Mac Exclusionary List or the FHFA Suspended Counterparty Program
- (g) The existence, sufficiency or enforceability of any required insurance or guaranty, or
- (h) The form and/or execution of Freddie Mac required Mortgage documents that without which make the Mortgage ineligible for sale or limit the enforceability of the required Mortgage terms (e.g., Uniform Residential Loan Application, power of attorney, Texas 50(a)(6) Mortgage documents or nonstandard and special purpose documents, such as Living Trusts)

PROCESS FOR REMEDYING ORIGINATION DEFECTS

The steps described below provide an overview of the process developed in support of the remedies framework that Freddie Mac will follow to categorize Defects, allow Corrections of Defects and remedy Defects through either a repurchase request or Repurchase Alternative.

Step 1 – Identification of Findings, PALs and Significant Defects

After a full-file quality control review is completed, Freddie Mac will designate any Defect(s) as resulting in a Finding, PAL or Significant Defect. The scope of full-file quality control reviews is the same for performing loans and non-performing loans.

If Freddie Mac designates the Defect as resulting in a Finding, Freddie Mac will not require a Correction or a Remedy from the Seller/Servicer. However, Freddie Mac may request a data update from the Seller/Servicer.

If Freddie Mac designates the Defect as resulting in a PAL, the Seller/Servicer must pay to Freddie Mac the applicable delivery fee that should have been paid when the Mortgage was purchased by Freddie Mac had the true and accurate facts about the Mortgage been known at the time of purchase. Freddie Mac may not demand repurchase of a PAL and the Seller/Servicer may not voluntarily repurchase a PAL.

If Freddie Mac identifies a Significant Defect, it will require repurchase of the Mortgage or may offer the Seller/Servicer a Repurchase Alternative.

Freddie Mac also checks for data discrepancies (which could be independent of a full-file quality control review) that may result in the assessment of a delivery fee.

Step 2 – Correcting certain Significant Defects

During the appeals process described in Section 72.6, a Seller/Servicer has the right to provide a Correction of any Significant Defects. Any additional documentation or information that the Seller/Servicer provides is subject to the same standard of quality control review as the initial Mortgage file documentation.

The documentation submitted to correct a Significant Defect must be based on information or data that either:

- Was available at the time of underwriting (and no later than the Note Date), or
- Covers the time of underwriting so long as such evidence meets the applicable documentation requirements set forth in the Purchase Documents

Seller/Servicers have the ability to correct Defects during the appeals process related to property, flood or mortgage insurance.

If a Seller/Servicer does not repurchase the loan or perform any Repurchase Alternative in accordance with the Purchase Documents, such Seller/Servicer continues to have the obligation to correct any Significant Defect in accordance with the Purchase Documents.

Step 3 – Freddie Mac review of Seller response and Mortgage reassessment

During the appeals process described in Section 72.6, Freddie Mac will conduct a Mortgage reassessment by reviewing any Corrections submitted by the Seller/Servicer in accordance with the applicable Purchase Documents in order to determine whether a Significant Defect still exists.

If a Seller/Servicer submits additional documentation and/or information, or takes steps which correct all Significant Defects in accordance with the Purchase Documents, Freddie Mac will rescind the Remedy request.

If, following reassessment, all Significant Defects have not been corrected in accordance with the Purchase Documents; the Seller must comply with the Remedy request in a timely manner.

If, following reassessment, Freddie Mac determines that the Mortgage is a PAL, the Seller/Servicer must pay Freddie Mac the delivery fee that should have been paid when the Mortgage was purchased by Freddie Mac had the true and accurate facts about the Mortgage been known at the time of purchase.

Freddie Mac may consider a Mortgage with a Significant Defect for a Repurchase Alternative depending on Freddie Mac's commercially reasonable determination that the Mortgage is retainable. Freddie Mac will determine whether the Mortgage is retainable based on the Seller/Servicer's Counterparty Status and whether the Mortgage was an acceptable investment at the time of purchase.

If a Repurchase Alternative is offered on a Mortgage with a Significant Defect, the Seller/Servicer can conclude that a full-file quality control review has been completed. However, if a Repurchase Alternative is offered on a Mortgage where a Seller/Servicer self-reports a Defect, the Seller/Servicer cannot conclude that a full-file quality control review has occurred nor is representation and warranty relief granted.

At any time during the appeals process, a Seller/Servicer has the right to propose a Repurchase Alternative following the identification of a Significant Defect. Freddie Mac will in good faith consider and respond to the Seller/Servicer's proposed Repurchase Alternative.

Freddie Mac may offer, or decline to offer, the Seller/Servicer certain Repurchase Alternatives based on the Seller/Servicer's Counterparty Status to the extent there are future obligations required as part of the Repurchase Alternative. Other factors to be considered by Freddie Mac may include, but are not limited to, the failure to maintain a quality loan origination process and the Seller's ability and willingness to comply with other provisions of the Purchase Documents.

If a Mortgage has multiple Significant Defects, and the Seller/Servicer is successful in correcting some, but not all of the Significant Defects, Freddie Mac may continue to pursue repurchase as a Remedy if the Mortgage has Significant Defects after the Mortgage reassessment is complete. If a Mortgage has multiple Significant Defects and the Seller/Servicer is successful in correcting all of them, but there remains a defect that makes the Mortgage a PAL after reassessment, Freddie Mac may subsequently notify the Seller/Servicer of the delivery fee that remains due.

Step 4 – Range of possible outcomes

Finding

If the Mortgage has had a full-file quality control review completed with only Findings discovered, the Mortgage will receive selling representation and warranty relief, subject to Section 6.14 (“representation and warranty relief”). If a Mortgage has not had a full-file quality control review, it may still receive representation and warranty relief through other provisions under the representation and warranty framework described in Section 6.14.

PAL

The appeals process for a PAL will result in one of the following outcomes:

- Rescission of the request for the payment of the delivery fee, or
- Payment of the delivery fee

If the PAL has had a full-file quality control review completed without the identification of any Significant Defects, the Mortgage will receive representation and warranty relief when the Seller/Servicer pays the delivery fee. Mortgages that have not had a full-file quality control review will not receive representation and warranty relief, even upon the payment of a delivery fee, but may still receive relief through other provisions under the representation and warranty framework.

Significant Defects

The appeals process for Mortgages with Significant Defects may result in a range of outcomes, including:

- Rescission of the Remedy request
- Agreement on a Repurchase Alternative, or
- Fulfillment of the Remedy request

If Freddie Mac offers a Repurchase Alternative after a repurchase demand has been issued, the Seller/Servicer has the option to repurchase the Mortgage instead of accepting the Repurchase Alternative.

If a Mortgage with a Significant Defect has had a full-file quality control review, it will receive representation and warranty relief if (i) all Significant Defects have been corrected, or (ii) a Repurchase Alternative has been offered and accepted and fully executed and completed by the Seller/Servicer in compliance with any related terms, including the expiration of all applicable time frames.

TOOLS TO SUPPORT THE SELLING REPRESENTATION AND WARRANTY FRAMEWORK

As a reminder, [Quality Control Information Manager \(QCIM\)](#) provides Seller/Serviceers with a single online end-to-end solution to manage performing and non-performing Mortgages through the quality control process. With QCIM, Seller/Serviceers have direct and timely access to the status of quality control loan file requests and all Freddie Mac repurchase and other remedy requests, including appeals. Freddie Mac’s repurchase letters will continue to detail the specific significant defects found during the quality control review, which will assist Sellers in preparing a detailed response. Additionally, Seller/Serviceers can use [Freddie Mac Loan Coverage Advisor[®] \(LCVASM\)](#) to calculate and track the representation and warranty relief date for any Mortgage sold to Freddie Mac.

REVISIONS TO THE GUIDE

The following Guide sections have been amended to reflect the changes announced in this Bulletin:

- 46.1, *Postfunding Quality Control*
- 72.1, *Repurchases Required by Freddie Mac Due to Violations of Selling and Origination Representations and Warranties*
- 72.2, *Repurchases Requested by the Seller/Serviceer*

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- *72.6, Appealing a Repurchase Request Due to Violations of Selling and Origination Representations and Warranties*

CONCLUSION

If you have any questions about the changes announced in this Bulletin, please contact your Freddie Mac representative or call Customer Support at (800) FREDDIE.

Sincerely,



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Single-Family Sales and Relationship Management